

1 UNITED STATES DEPARTMENT OF AGRICULTURE
2 BEFORE THE SECRETARY OF AGRICULTURE

3 IN re: Docket #AO-F&V-991-A3; FV03-991-01
4 HOPS PRODUCERS FOR WASHINGTON, OREGON, IDAHO AND
5 CALIFORNIA
6

7 Hearing held on the 20th day of October, 2003
8 at 8:30 a.m.

9 Doubletree Hotel Yakima Valley
10 1507 North 1st Street
11 Yakima, Washington 98901
12

13 TRANSCRIPT OF PROCEEDINGS
14

15
16 BEFORE: HONORABLE JILL S. CLIFTON

17
18 FOR PROPONENTS:

19 BRENDAN MONAHAN, ESQUIRE

20 FOR OPPONENTS:

21 JAMES MOODY, ESQUIRE
22
23

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P R O C E E D I N G S

October 20, 2003

ADMINISTRATIVE LAW JUDGE: We're on record now.

It's 8:50 in the morning on Monday, October 20, 2003.

This is a continuation of the Hops rule-making hearing that began last week in Portland, Oregon. We're now in Yakima Washington. I'd like to read into the record the case caption. The case caption is IN RE: HOPS PRODUCED IN WASHINGTON, OREGON, IDAHO, AND CALIFORNIA. The

Docket Number is AO-F&V-991-A3;FV03-991-01. The transcript being produced, which will contain the witnesses' testimony and all of our other oral record made in this hearing is divided into volumes. Each day has a different volume. Today is Volume IV and the numbers in the transcript should be sequential to those of last week, so where we left off Friday night should be where we begin with page numbers for this volume. My name is Jill Clifton. I'm a United States Administrative Law Judge and I'm assigned to the rule-making hearing for the purpose of gathering in the evidence and then certifying that record to the Secretary. The decision in this case will be that of the Secretary of Agriculture. There are two types of evidence, testimony, and exhibits. We're already in the process in this hearing, and so much of the evidence is

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1 already in. We've taken testimony of witnesses and
2 we've taken in exhibits. Some of those witnesses will
3 testify again here, some presented only direct
4 examination in Portland. They'll be here for cross-
5 examination. For the purpose of the record, you must
6 assume that we're starting anew, including identifying
7 yourself completely the first time you're asked to
8 speak, spelling your names as well as saying them, and
9 then if you are going to testify again, identifying
10 yourself fully and spelling your name. If you use a
11 term that might not be familiar to people who are not
12 familiar with the hops industry and are not familiar
13 with this community, please pause and spell that for us,
14 too. Names like names of the varieties of hops or names
15 like the community Toppenish, for example. Most people
16 who are not from here might misspell it. So if you'll
17 just take that in mind and remember that we want the
18 written record to be accurate. I'd like now to begin
19 with the identification of the people who are seated at
20 the tables and I'll start with the table that is to my
21 right and then I will go to the table that is to my
22 left, then I'll go to the table that is across the room
23 and begin at my right.

24 MS. DESKINS: My name is Sharlene Deskins.
25 First name is spelled S-h-a-r-l-e-n-e. The last name is

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1 spelled D-e-s-k-i-n-s. I'm an attorney with the United
2 States Department of Agriculture Office of General
3 Counsel. I represent the Agricultural Marketing Service
4 in this case.

5 MS. DEC: Good morning. My name is Anne Dec.
6 It's spelled A-n-n-e D-e-c. I'm with USDA's
7 Agricultural Marketing Service in Washington, DC.

8 MS. FINN: Kathleen Finn, K-a-t-h-l-e-e-n
9 F-i-n-n. I'm with USDA's Agricultural Marketing Service
10 in Washington, DC.

11 DR. HINMAN: Donald Hinman. D-o-n-a-l-d
12 H-i-n-m-a-n. Economist with Agricultural Marketing
13 Service, USDA, in Washington, DC.

14 MR. BROADBENT: Barry Broadbent, AMS,
15 stationed in Portland Northwest Marketing Field Office.

16 ADMINISTRATIVE LAW JUDGE: Spell your name,
17 please.

18 MR. BROADBENT: Broadbent. Barry Broadbent,
19 B-a-r-r-y B-r-o-a-d-b-e-n-t.

20 MR. OLSON: My name is Gary Olson. G-a-r-y
21 O-l-s-o-n. I'm regional manager of the Northwest
22 Marketing Field Office, Portland, Oregon.

23 MR. MONOHAN: Brendan Monahan, attorney for
24 the proponent's committee. B-r-e-n-d-a-n M-o-n-a-h-a-n.

25 MR. CARPENTER: Stephen Carpenter.

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1 S-t-e-p-h-e-n C-a-r-p-e-n-t-e-r. Member of the
2 proponent's committee.

3 MR. ROY: Leslie Roy. L-e-s-l-i-e R-o-y, last
4 name. Proponent farmer from Yakima Valley.

5 MR. GASSELING: Tom Gasseling. It's Thomas W.
6 Gasseling. T-h-o-m-a-s W. Gasseling, G-a-s-s-e-l-i-n-g.
7 Proponents committee farmer from Wapato, Washington.
8 W-a-p-a-t-o.

9 ADMINISTRATIVE LAW JUDGE: Could everyone in
10 the back hear that? Raise your hand if you could not
11 hear. All right, good.

12 MR. DESSERAULT: Ken Desserault. That's K-e-n
13 D-e-s-s-e-r-a-u-l-t, grower, state of Washington.

14 MR. BRULOTTE: Reggie Brulotte, R-e-g-g-i-e
15 B-r-u-l-o-t-t-e, grower, Toppenish, Washington.
16 T-o-p-p-e-n-i-s-h.

17 ADMINISTRATIVE LAW JUDGE: And Mr. Moody, if
18 you'd now...

19 MR. MOODY: All right. Jim Moody, Washington,
20 DC. M-o-o-d-y. Counsel for the opposing growers.

21 MR. CARSWELL: Matthew Carswell,
22 M-a-t-t-h-e-w C-a-r-s-w-e-l-l, in-house counsel for
23 Anheuser-Busch Companies, Inc. That's A-n-h-e-u-s-e-r -
24 B-u-s-c-h Companies, Inc. Anheuser-Busch is an opponent
25 of the proposed order.

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1 DR. JEKANOWSKI: Mark Jekanowski. I'm an
2 economist with Sparks Companies, Incorporated. My name
3 is spelled M-a-r-k J-e-k-a-n-o-w-s-k-i.

4 DR. TWEETEN: Luther Tweeten, L-u-t-h-e-r
5 T-w-e-e-t-e-n, Professor Emeritus at Ohio State
6 University and representing the opposition.

7 ADMINISTRATIVE LAW JUDGE: And now, what is
8 your most advanced degree?

9 DR. TWEETEN: Ph.D.

10 ADMINISTRATIVE LAW JUDGE: Thank you, Dr.
11 Tweeten. All right, there are a number of you who have
12 not yet identified yourselves, but you expect to be
13 calling witnesses, questioning witnesses, or testifying
14 today. If that is the case, I'd like you to come
15 forward and identify yourself now, even though you will
16 also identify yourself at a later time. So if you will
17 come to a -- come near a place where there is a
18 stationary microphone, because I want you to be near the
19 amplification mike, as well as the recording mike. If
20 you would do that at this time.

21 MR. FOLWELL : Ray Folwell, R-a-y
22 F-o-l-w-e-l-l, Washington State University, Pullman.
23 P-u-l-l-m-a-n.

24 ADMINISTRATIVE LAW JUDGE: And what is your
25 most advanced degree?

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1 DR. FOLWELL: Ph.D.

2 ADMINISTRATIVE LAW JUDGE: Thank you, Doctor.

3 MR. CHRISTENSEN: Rod Christensen, R-o-d
4 C-h-r-i-s-t-e-n-s-e-n. I'm a consultant working for the
5 proponent committee.

6 MR. CHANDRAMAZUMDAR: J. Chandramazumdar.
7 J. C-h-a-n-d-r-a-m-a-z-u-m-d-a-r, Attorney, United
8 States Department of Justice, Antitrust Division.

9 MR. HARMONEIS: Michael Harmoneis,
10 H-a-r-m-o-n-e-i-s. I'm also an attorney with the
11 Department of Justice.

12 ADMINISTRATIVE LAW JUDGE: All right, thank
13 you. As far as our timetable for proceeding, we were
14 fearful that we might have to work late while we were in
15 Portland in order to get all the evidence in. We just
16 worked a little late a couple of the nights, but we
17 didn't work late late. This week, we again may have to
18 work late in order to get all the evidence in. I'm
19 hopeful not, but I want everyone to keep me apprised as
20 to when you might suggest that we go late to serve the
21 convenience of a witness or because there's a topic that
22 we're in that we need to finish before we move to the
23 next topic, or the like. Because this is a public
24 hearing, I invite the input of anyone who has a
25 suggestion as to how we might proceed. We want, most of

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1 all, to accommodate growers who want to be heard, either
2 in favor of the proposals or against them, who need to
3 go back to their everyday chores. So if you're a grower
4 and you want to be heard and you don't know a contact
5 within those people who've identified themselves so far,
6 you may just come to a microphone and let us know that
7 you would like to be heard so that you can promptly
8 return your other responsibilities. Also, I want you to
9 know that the court reporter is named Kearney Barton.
10 That's spelled K-e-a-r-n-e-y, Barton, B-a-r-t-o-n. He
11 advises me that we can call him Kearney and I'm going to
12 ask him at this time to interrupt at any time for any
13 reason. I know that he'll interrupt to change the
14 tapes, which must be done at about 45-minute intervals.
15 If you're stopped in the middle of a sentence, if you
16 have something where you can just jot down a note as to
17 where you were, so that when we get back on record you
18 can repeat that thought and we can go on from there. So
19 if you're a witness at the witness stand, I invite you
20 to bring up a pencil and notepad. It may help you keep
21 track of the thoughts that you wanted to express because
22 you may be interrupted, not only to change the tape, but
23 also because someone may have an objection to where
24 we're going with the testimony. The other reason it's a
25 good idea to keep pen and pad is there were a number of

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1 hypothetical questions asked and the witnesses did great
2 keeping all the numbers in their heads, but had it been
3 me, I'd have needed a pen and a pad. Now, preliminary
4 matters that others would like to raise -- we will break
5 for lunch at some time. I'd like to be guided by the
6 people who are putting on evidence at that time as to
7 when they suggest that we break. We'll also take a
8 break in the morning, one or more, and a break in the
9 afternoon, one or more, for comfort. All right. Any
10 other preliminary matters? Ms. Deskins?

11 MS. DESKINS: Judge Clifton, since we are at a
12 new hearing site, I did want to say on the record that
13 the government hasn't taken a position on this matter.
14 We're here to gather evidence and also that the ex-party
15 rules under the 700 rules -- I'm sorry, the 900 rules of
16 practice applies and we cannot discuss the merits of the
17 case with anybody. Thank you.

18 ADMINISTRATIVE LAW JUDGE: Thank you, Ms.
19 Deskins. And Ms. Deskins, that applies to everyone
20 seated at the same table as you, is that correct?

21 MS. DESKINS: Yes, Your Honor. It applies to
22 everyone here seated at the table. It also applies to
23 you, Judge Clifton.

24 ADMINISTRATIVE LAW JUDGE: Thank you. Now,
25 you may need to approach me about scheduling matters and

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1 I welcome that. It's easier, though, if you wait until
2 we're all on the record, because I'm going to have to
3 have you do it again, anyway, in order to let everyone
4 voice favor or opposition to that. But if you want to
5 give me a heads-up, that's fine. All right, any other
6 preliminary matters? All right, Mr. Monahan, I
7 interrupted your presentation many times last week and I
8 hope that I will not have to do that as often now that
9 we're here. And would you like now to proceed?

10 MR. MONAHAN: I would, Your Honor, thank you.
11 Can you hear me with this lapel microphone?

12 ADMINISTRATIVE LAW JUDGE: I can hear you,
13 but...

14 MR. MONAHAN: Do I need to hold it up to my
15 mouth?

16 ADMINISTRATIVE LAW JUDGE: I think so. I'm
17 sorry. That's...

18 MR. MONAHAN: How about that? Is that better?

19 ADMINISTRATIVE LAW JUDGE: That's great.

20 MR. MONAHAN: Okay.

21 ADMINISTRATIVE LAW JUDGE: Can you hear him in
22 the back? Stand up if you can hear him in the back.

23 MR. MONAHAN: Oh. We got a wave. I think
24 we're all right, Your Honor.

25 ADMINISTRATIVE LAW JUDGE: Okay, good.

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1 MR. MONAHAN: Your Honor, when we last spoke,
2 we had been talking about a new definition for the term
3 handle, which is set forth at 900. -- I believe --
4 excuse me, 991.08. That, I would announce to the court,
5 is still a work-in-progress. That is something that we
6 will be presenting through a witness, but not first
7 thing. When we heard the persons introduce themselves
8 this morning, we heard the term doctor, I want to say
9 four times. I've spoken to Mr. Carswell. We want to
10 take advantage of the presence today of economists, and
11 I believe that the proponents are going to start out
12 with Dr. Folwell, who will offer testimony regarding
13 economic justification for the proposed order, and I
14 believe, with Mr. Carswell's agreement, we'll go right
15 into Dr. Jekanowski and Dr. Tweeten and have today be a
16 day that perhaps only Dr. Hinman would love and that is
17 a focus on economics.

18 ADMINISTRATIVE LAW JUDGE: I think to the
19 contrary. I really think the economists' testimony is
20 going to be extremely interesting. So don't disappoint
21 me, men.

22 MR. MONAHAN: Mr. Carswell, is that a -- can
23 we agree that that's the approach we'll take today?

24 MR. CARSWELL: Actually, I think we should ask
25 Jim, but I certainly am amenable to that, Brendan.

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1 MR. MOODY: Yeah, that's fine, Brendan. Thank
2 you.

3 ADMINISTRATIVE LAW JUDGE: All right, good.
4 Then you may call your first economic witness.

5 MR. MONAHAN: Thank you, Your Honor. And
6 first -- and I believe from our standpoint, only. Dr.
7 Folwell.

8 ADMINISTRATIVE LAW JUDGE: Dr. Folwell, do you
9 want to pour yourself some water before you get started?

10 DR. FOLWELL: No, I'm fine. Thank you.

11 ADMINISTRATIVE LAW JUDGE: All right. Would
12 you state your full name again for the record and spell
13 your names, please?

14 DR. FOLWELL: Raymond J. Folwell,
15 R-a-y-m-o-n-d J. F-o-l-w-e-l-l.

16 ***

17 RAYMOND J. FOLWELL,
18 having first been duly sworn, according to the law,
19 testified as follows:

20 ***

21 DIRECT EXAMINATION

22 BY MR. MONAHAN:

23 Q. Thank you, Your Honor. Dr. Folwell,
24 could you just briefly introduce yourself to those of us
25 here. Tell us who you are and what you do?

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1 A. I'm a Professor of Agriculture and
2 Resource Economics at Washington State University and
3 director of the Viticulture and Enology program also for
4 the university. I've been there for 35 years. This is
5 my 36th year. I've taught a wide array of courses. I
6 work in numerous areas concerning research and
7 extension, of which one of them is the area of hops.

8 Q. Could you briefly describe your
9 educational background, sir?

10 A. I have a Bachelor's Degree, a
11 Baccalaureate Degree from the University of Illinois, a
12 Masters of Science and Agricultural Economics from the
13 University of Illinois, and a Ph.D., Doctor of
14 Philosophy in Agricultural Economics from the University
15 of Missouri.

16 Q. In this case you were asked by the
17 proponents' committee to address the issue of whether
18 there's a need for a federal marketing order in hops,
19 were you not?

20 A. That's correct.

21 Q. And to that end did you prepare a report?

22 A. Yes, I did.

23 Q. And I sent you to the copy machine early
24 and often, did I not?

25 A. Well, I made copies.

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1 ***

2 ADMINISTRATIVE LAW JUDGE: Let's go off record
3 while those copies are distributed. It's now 9:10. Off
4 the record before you...

5 ***

6 [Off the Record]

7 [On the Record]

8 ***

9 ADMINISTRATIVE LAW JUDGE: We're back on
10 record at 9:15. I know you haven't finished reading the
11 report, but I'm reminded of one other housekeeping item
12 that I wanted to do before we went on record. I wanted
13 to make a record of the exhibits that we have here in
14 the hearing room and hand those now to Mr. Kearney.
15 Some of these have been admitted and some have not, but
16 we have them presently here and I'd like to call on Ms.
17 Dec to now identify those that we have as part of the
18 official record.

19 MS. DEC: Yes, Your Honor. I have 25 exhibits
20 that were presented at the session last week in
21 Portland. All but five exhibits, 11 through 15, were
22 admitted into evidence.

23 ADMINISTRATIVE LAW JUDGE: All right,
24 excellent. Would you now hand all 25 of those to the
25 court reporter?

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1 MS. DEC: Yes, ma'am.

2 ADMINISTRATIVE LAW JUDGE: All right, I'd like
3 to proceed now, even though many of you will still be
4 looking at the report through the direct examination.
5 Mr. Monahan, you may begin.

6 MR. MONAHAN: Thank you, Your Honor. The
7 first thing I'd like to do is to have Dr. Folwell's
8 report, entitled "Is There a Need for a Federal
9 Marketing Order in Hops?". The marking has
10 identification 26.

11 ADMINISTRATIVE LAW JUDGE: Yes. Would you
12 hand that to the court reporter? I'm going to mark it
13 as Exhibit 26.

14 MR. MONAHAN: Thank you.

15 ADMINISTRATIVE LAW JUDGE: You're welcome.

16 ***

17 BY MR. MONAHAN:

18 Q. Now, Dr. Folwell, before I ask you
19 questions about this report, I'd like to talk to you a
20 little bit about your background. There has been some
21 discussion and debate in this matter regarding the
22 previous hop marketing order. I'd like to ask if you
23 have any experience under the operation of that hop
24 marketing order?

25 A. Under the previous hop marketing order
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1 No. 991, I believe it was, I was the public
2 representative on that federal marketing order.

3 Q. What did the public representative do?

4 A. I usually like to paraphrase that I was
5 protecting the interests of the beer drinkers of America
6 and around the world, but basically, I was there to
7 provide a service to make sure that the administrative
8 committee was operating in an acceptable manner in terms
9 of attempting to balance the supply and demand of hops
10 to the market.

11 Q. And how did you do that as a practical
12 matter?

13 A. As a practical matter, at each meeting
14 there was a statistical sub-committee of the
15 administrative committee which would provide projections
16 of the various components of supply and demand. Each
17 member of the administrative committee then would have
18 an opportunity to raise questions, to give their input
19 into the ideas. Then there would usually be a
20 recommendation on the saleable percentage based upon the
21 balance sheet approach they were using to this and then
22 they would ask my opinion on whether or not I thought
23 the projections were reasonable and accurate.

24 Q. What years did you play that role?

25 A. I believe from about late 1978 or '79

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1 until the termination of the order in 1986.

2 Q. Is it fair to say that one of the roles
3 or duties of the statistical sub-committee was to
4 project demand for hops?

5 A. Yes, it was.

6 Q. And based on your experience and
7 observations, how did they do that?

8 A. They had a wealth of information. As a
9 matter of fact, the hop growers in the US had more
10 market information available to them through the
11 marketing order than any other agricultural industry I'm
12 aware of and they would basically look at the trends for
13 each of the components of demand, both domestic and
14 foreign and then make projections based upon those
15 trends.

16 Q. And what is your recollection as to how
17 accurate the statistical sub-committee was with respect
18 to projecting demand for hops?

19 A. If they were taking a course from me in
20 this, I would give them an A. They were very accurate,
21 they carried out their responsibilities in a very
22 serious manner. They had input from various sources.
23 They even contacted sources for what was going on in
24 Europe and around the world.

25 Q. In the course of your duties as -- you
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1 have to remind me of your title, sir, again with the
2 previous order.

3 A. Public representative.

4 Q. In the context of your role as public
5 representative, and with your background in economics,
6 did you have the opportunity to draft or author any
7 materials regarding the volume regulations contained in
8 the prior order?

9 A. Yes, I did.

10 Q. Can you describe those for us, please?

11 A. Basically, in the early -- probably
12 starting in about 1980, I was somewhat, you know,
13 concerned about the fact that the administrative
14 committee, with a recommendation of the Secretary of
15 Agriculture could influence the flow of hops to the
16 market, so basically, I undertook a research project at
17 Washington State University which attempted to analyze
18 their projections in relation to the actual market
19 outcomes.

20 Q. Sir, I'm going to hand to you three
21 documents that I just got my hands on this morning out
22 of your briefcase. Could you describe those or identify
23 those for the record, sir?

24 A. The first one in a technical research
25 bulletin published by Washington State University, No.

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1 97. It was published in 1982. It is entitled "The
2 United States Hop Industry and the Volume Control
3 Provisions of the United States Federal Hop Marketing
4 Order", of which I was the principal author.

5 ***

6 MR. MONAHAN: Just -- to make it clear for the
7 record, Your Honor, I would like to have these three
8 documents marked for identification before I have the
9 Doctor speak about them.

10 ADMINISTRATIVE LAW JUDGE: All right. Thank
11 you.

12 MR. MOODY: Brendan, do you have copies of
13 those available?

14 MR. MONAHAN: I don't yet, but we'll have to
15 do some quick copying in one of the breaks.

16 MR. MOODY: Thank you.

17 MR. MONAHAN: I apologize for that.

18 ADMINISTRATIVE LAW JUDGE: I am marking as
19 Exhibit 27 "United States Hop Industry and the Volume
20 Control Provisions of the United States Federal Hop
21 Marketing Order" by R.J. Folwell, P.K. Hennessy -- and
22 that's the initial P., the initial K., H-e-n-n-e-s-s-y,
23 R.K. Mittlehammer -- the initial R., the initial C.,
24 excuse me. I said K., I think. It's R.C. Mittlehammer.
25 The initial R., the initial C., M-i-t-t-l-e-h-a-m-m-e-r.

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1 And A.H. Harrington, the initial A., the initial H.,
2 Harrington, H-a-r-r-i-n-g-t-o-n, Agricultural Research
3 Center, Washington State University. And then there's
4 an identification that says XT0097, 1982. Exhibit 28 is
5 a booklet entitled "Department of Agricultural
6 Economics" Washington State University, Pullman,
7 P-u-l-l-m-a-n, Washington. That is by Raymond J.
8 Folwell, dated April 15, 1982. Exhibit 29 is a
9 publication entitled "Agricultural Economics Research -
10 Fall, 1985, Volume 37, No. 4." It is a journal of the
11 United States Department of Agriculture Economic
12 Research Service. Thank you, Mr. Monahan. I've marked
13 these, but you may now return them to the witness.

14 ***

15 BY MR. MONAHAN:

16 Q. Thank you, Your Honor. Dr. Folwell, I'd
17 just like to go through these documents briefly, and in
18 turn have you describe what they are, what the purpose
19 of the project was and your conclusions?

20 A. Basically, this is the research project
21 which I indicated I undertook, probably starting in
22 about 1980. It consisted of a master's thesis by
23 Patrick Hennessy, in which we analyze the projections of
24 the supply and demand components made by the hop
25 administrative committee and compared them to the actual

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1 market results for each year.

2 Q. And what did you conclude?

3 A. On page six of the report I prepared,
4 about halfway down the page there's a summary statement
5 that indicates that the analysis revealed that on the
6 average, the committee overestimated demand components
7 and underestimated supply components. The HAC, being
8 the Hop Administrative Committee, can best be described
9 as being "overly optimistic in their decision process
10 and placing on the market a larger quantity than needed
11 if they had perfect knowledge and were able to project
12 all supply and demand components with complete accuracy.
13 As a result, it can be partially concluded that the HAC
14 did not unduly use its market power in restricting the
15 quantity of hops available to the market from domestic
16 production."

17 Q. Would that be a fair way to summarize the
18 identifications 26, 27, and 28?

19 A. I believe so.

20 Q. Okay. Sir, were you -- do I understand
21 that you were involved with the hop marketing order and
22 with the administrative committee in the final years of
23 its operation, early mid '80s?

24 A. Correct.

25 Q. You were around when the -- really, at
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1 the termination of the earlier order.

2 A. I was there, yes.

3 Q. Are you able to describe, from your
4 experience and recollection, why the earlier order was
5 terminated?

6 A. Actually, I think there were a lot of
7 factors that contributed to it. One was the lack of
8 foresight, both by the hop industry as well as the hop
9 dealers and buyers of hops, that a crop failure in the
10 Hallertau region of Europe, primarily Czechoslovakia and
11 Germany, was going to lead to the demise of the hop
12 industry in Europe. There was an overreaction on the
13 part of all parties, including dealers, growers, buyer
14 of hops, to over plant hops in the US. Also, at the
15 same time -- and this happened in the fall of 1979 --
16 the price of spot hops, those not under contract, went
17 from 75 cents a pound to \$6 a pound overnight and greed
18 sat into this industry. The value of base and allotment
19 went up and there were a number of lawsuits filed
20 concerning the operation of the federal marketing order,
21 and it was just a matter of greed that I think really
22 led to the termination of the order.

23 Q. There's been some discussion and
24 conflicting testimony as to whether the prior order was
25 a success or a failure, Dr. Folwell, and I'd like to ask

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1 you, as a representative who worked on the order and
2 your professional opinion as a Ph.D. economist, was the
3 prior order a success or a failure?

4 A. I think it was a success as long as the
5 industry continued to use the accounting balance sheet
6 approach that they used in terms of projecting supply and
7 demand and making sure that supply and demand were in
8 balance and when they did this on an annual basis.

9 Q. And just in general terms, when the
10 industry was able to do that, why was it a success? Why
11 did it succeed?

12 A. Basically, because the industry was
13 placing enough hops on the market to meet both domestic
14 and foreign demand and they also had a basic philosophy,
15 if you go back and read the minutes of the Hop
16 Administrative Committee, their basic philosophy was
17 that they wanted to capture a larger share of the
18 market, both domestically and worldwide.

19 Q. Sir, I'd like you to turn then to Exhibit
20 26, which is your most recent report entitled "Is There
21 a Need for a Federal Marketing Order in Hops?" and if
22 it's not too big an imposition, I'd like you to read it
23 into the record.

24 A. The entire document or paraphrase it?

25 Q. Well, I will invite you to paraphrase it.

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1 Others may ask for more detail.

2 A. Okay. Maybe it would be best if I just
3 read it. "The hop plant is a perennial that requires a
4 substantial capital investment to establish a hop yard.
5 Hops are marketed under multiple year contracts at fixed
6 prices which also make hops unique from most other
7 agricultural products. The sum of the establishment and
8 the first year costs per acre that are required before a
9 mature hop yard is in full production are \$7,732 for
10 aroma hops, \$7,773 for alfalfa hops, \$8,063 for super
11 alpha hops, and these are based upon 1999 input costs.
12 Producers are reluctant to make such large capital
13 investment unless there is an expectation of a
14 reasonable and stable market demand and profits for the
15 product. In the past, the stability has been
16 demonstrated by the percent of hops sold or contracted
17 ahead. This percentage has been slowly declining.
18 Without the use of some type of marketing tools,
19 including a marketing order, the US hop industry will
20 continue to fact a state of chaos. A major indicator of
21 the chaotic state has been the decreasing number of hop
22 producers and dealers. Towards the end of the last hop
23 marketing order in the mid-1980s, there were 211 base
24 holders or producers. Today, without a federal
25 marketing order, the number of producers has declined to

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1 about 70. In relation to the number of buyers or
2 dealers, the numbers has [sic] decreased from nine in
3 1986 to only four in 2003, with one of those four being
4 a grower cooperative. Thus...

5 ***

6 ADMINISTRATIVE LAW JUDGE: Dr. Folwell, I
7 don't want to interrupt. You've been going very fast.
8 I just want you to go back to where you talked about the
9 cost.

10 DR. FOLWELL: Yes, ma'am.

11 ADMINISTRATIVE LAW JUDGE: And I thought you
12 said alfalfa hops.

13 DR. FOLWELL: Did I? That could be.

14 ADMINISTRATIVE LAW JUDGE: I just want you...

15 DR. FOLWELL: Alpha.

16 ADMINISTRATIVE LAW JUDGE: ...to go back over
17 the numbers and the types of hop again, if you will.

18 DR. FOLWELL: Okay. \$7,732 for aroma hops,
19 \$7,773 for alpha hops, and \$8,063 for super alpha
20 hops...

21 ADMINISTRATIVE LAW JUDGE: All right...

22 DR. FOLWELL: ...based upon '99 costs.

23 ADMINISTRATIVE LAW JUDGE: ...thank you.

24 DR. FOLWELL: Continuing on down the page. I
25 just -- starting from the fifth line from the bottom.

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1 "Thus, while there has been increasing concentration of
2 the hop growers on the supply side of the market, there
3 has been even further concentration in the number of
4 dealers on the demand side of the market. These trends
5 suggest that there has been increasing market power on
6 the demand side of the market relative to the supply
7 side with producers losing market power. Such an
8 imbalance in market power is not a desirable economic
9 situation. A federal marketing order would provide the
10 opportunity for growers to regain some of their market
11 power. The countervailing market power that a federal
12 marketing order with a producer allotment provision
13 would provide will help bring stability to the US hop
14 industry. The US hop industry seeks to lessen the
15 chaotic state and instability that it currently finds
16 itself in through a federal marketing order. It is
17 anticipated that the federal marketing order 1) achieve
18 greater stability of hop farm income. 2) Increase hop
19 prices in the long run. 3) Transfer some market power
20 and decision making from hop dealers to hop growers,
21 i.e., greater participation in the marketing process by
22 hop grower, and 4) generate market information and
23 research contributing to improved market understanding
24 and decision making by US hop growers." There's a
25 heading "Why a Federal Marketing Order?". "One of the

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1 primary objectives of the Federal Marketing Order is the
2 creation of an orderly marketing system, which according
3 to Kohls and Uhl is "the coordination of the total
4 supply of a commodity over time, form, and spatial
5 markets, in such a way as to achieve some market
6 objectives." The US hop industry is in need of an
7 orderly marketing program since the structural supply
8 and demand for US hops is inelastic with respect to
9 price. This inelasticity results in wide price swings
10 with very small changes in the quantity supplied or
11 demanded. The inelasticity of the supply and demand for
12 US hops is fully documented in the classic study by
13 Habuki. Habuki found that "the elasticity of the spot
14 market price with respect to the total US hop production
15 is a -3.382 [sic]. This implies that a one percent
16 increase in total hop production will decrease the
17 market price by almost 3.34 percent." These research
18 results indicate an inelastic demand with respect to
19 price in the short run for hops. Habuki estimates that
20 the short run supply elasticities with respect to price
21 are .0500, .0549, and .052 [sic] with respect to prices
22 lagged one, two, and three years respectively. Habuki
23 estimates the long run supply elasticities to be .05579,
24 and .0613, and .0587 with respect to prices lagged one,
25 two, and three years respectively. These results

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1 indicate an inelastic supply of US hops. The above
2 results are in direct contradiction to a report filed to
3 the USDA in a letter by Mark -- excuse my pronunciation
4 -- Jenakowski?

5 DR. JEKANOWSKI: Jekanowski.

6 DR. FOLWELL: Jekanowski, okay -- of Sparks
7 Companies, Incorporated, to Charles Parrot, Associate
8 Deputy Administrator of the USDA/AMS. In that report,
9 they -- being Sparks -- concluded that the demand with
10 respect to prices for alpha acid is elastic, i.e.,
11 reduce the quantity and the total revenue will decrease.
12 The Sparks model is a complete over-simplification of
13 the supply and demand structures of the US hop industry
14 and has serious statistical problems. In relation to
15 the economic simplicity of the model, such single
16 equation models estimated with ordinary least-squares
17 will always result in calculated elasticities of demand
18 with respect to price that are more elastic than models
19 that contain several equations involving simultaneous
20 relationships which are more reasonable representations
21 of actual market conditions. An example of the latter
22 is the work by Habuki. The Sparks model suffers from
23 serious statistical problems, including insignificant
24 explanatory variables and serial or autocorrelation.
25 First, one variable -- one explanatory variable, the Log

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1 of Beer Production, is not statistically significant and
2 should be dropped from the model. If this variable is
3 dropped from the model, the adjusted coefficient of
4 determination is increased marginally, but the serious
5 problem of autocorrelation or serial correlation still
6 remains. The Durbin-Watson statistic, DW, used to test
7 for autocorrelation with the original Sparks model is
8 0.55 and 0.48 with the deleted variable. The Durbin-
9 Watson statistic indicates that the single equation
10 model has positive autocorrelation resulting from a
11 specification error and/or wrong functional form,
12 linear, was used. A good researcher would not place any
13 degree of confidence in such research results.
14 Autocorrelation leads to a downward biased standard
15 errors and thus is incorrect and -- and thus to
16 incorrect statistical tests and confidence intervals.
17 However, the Sparks model goes on to use the model to
18 indicate that the demand for US hops is elastic. This
19 conclusion is based upon an unacceptable statistical
20 model. Further, the Sparks report fails to acknowledge
21 that the price flexibility coefficient only sets a lower
22 limit of the price elasticity of demand -- and there's a
23 reference to a standard text book. As indicated by
24 Tomek and Robinson, if there are no cross effects or
25 substitutes for a product, then the reciprocal of the

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1 price elasticity [sic] is a good approximation of the
2 elasticity. If significant cross effects exist, the
3 reciprocal of price flexibility is less than the demand
4 elasticity. In the case of the US hops or alpha acid
5 there exists a near substitution in the form of the same
6 product or products from Germany and other hop producing
7 countries. The Sparks model is not acceptable
8 statistically or economically. Given the sophistication
9 the Habuki model and the inclusion of the supply and
10 demand for hops from Germany, it must be concluded that
11 the demand for US hops is inelastic. To illustrate the
12 dynamic nature of the US hop market, the price of alpha
13 and alpha acid production, as taken from the Sparks
14 report, is graphed in figure one, which appears on page
15 eight of this report. Inspection of the scatter plot
16 where each point represents the intersection of a supply
17 and demand curve on an annual basis reveals a definite
18 pattern. The years 1977 to '79, 1980 to '83, 1986 to
19 1990, and 1991 to 2001 fall in four distinct cluster.
20 The clusters with contiguous years within each cluster
21 demonstrate the shifting of the demand and supply curves
22 for the US hops over time. Within each cluster, the
23 demand curve has been more stable than the supply curve.
24 The single equation model developed by Sparks failed to
25 account for these major shifts in demand. Therefore,

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1 the specification error indicated by the positive
2 autocorrelation is expected given the simple nature of
3 the model. If one were to fit a single equation to the
4 data set the shifts in the demand function must be
5 accounted for by binary variables to change the
6 intercept value for each time period defined by the
7 clusters. The model fit to the Sparks data with the
8 addition of the binary variables to account for the
9 shifts resulted in the following...

10 ADMINISTRATIVE LAW JUDGE: Could we go off the
11 record for a moment?

12 ***

13 [Off the Record]

14 [On the Record]

15 ***

16 ADMINISTRATIVE LAW JUDGE: We're back on
17 record now at 9:57. During the break Dr. Folwell gave
18 an extra copy of his report to the court reporter so the
19 court reporter can send that along with the tapes to
20 assist the typist. That's a very good technique and I
21 would appreciate it if any of you are going to be
22 reading a written statement into the record, if you can
23 provide an extra copy of that statement to the court
24 reporter, it does assist in transcription. All right,
25 Dr. Folwell, you may resume.

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1 DR. FOLWELL: Thank you. I'm on page five
2 about a third of the way down. I am not going to read
3 the equation and the definition of all the variables
4 into the record, but to paraphrase it, basically it's an
5 equation in which the alpha acid production, which
6 expresses a function of the real price of alpha, the
7 logarithm of years acting as a trend and three binary
8 variables to account for the shifts. Also, paraphrasing
9 the fit of this equation was extremely good with a
10 coefficient of determination an R2 of almost .9 as
11 compared to the Sparks model, which had one of .5.
12 Basically, we explained 90 percent of the variation in
13 the alpha acid production as a function of those
14 variables compared to only 50 percent with the Sparks
15 model and also that the Durbin-Watson statistic was
16 inconclusive in terms of testing for positive
17 autocorrelation. Reading again from the text starting
18 with the second line from the bottom on page five, that
19 paragraph, "given that the model reported above is a
20 double logarithm function form and the quantity variable
21 on the left hand side, the coefficient of $-.71456$ is the
22 direct price elasticity. This result indicates that the
23 demand for US hops is inelastic. These results are in
24 agreement with those of Habuki. In addition to the
25 wrong conclusion drawn by the Sparks model above, the

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1 elasticity of demand -- about the elasticity of demand
2 for US hops, the report repeats numerous times that the
3 purpose of the hop marketing order with a producer
4 allotment provision is to maximize total revenues to hop
5 growers. Past history of the US hop industry and its
6 constituents strongly suggest that such a behavior
7 pattern would not exist. An empirical analysis of the
8 behavior of the Hop Administrative Committee under
9 Federal Marketing Order 991 was conducted to determine if
10 the HAC restricted the flow of hops to the market. The
11 comparison was HAC's projected components of supply and
12 demand to actual market results. In published and
13 reviewed research concerning the behavior of the HAC
14 under the federal marketing order, it was concluded that
15 'The analysis revealed that on the average, the
16 committee overestimated demand components and
17 underestimated supply components. The HAC can best be
18 described as being overly optimistic in their decision
19 process projections and placing on the market a larger
20 quantity than needed if they had perfect knowledge and
21 were able to project all supply and demand components
22 with complete accuracy. As a result, it can be
23 partially concluded that the HAC did not unduly use its
24 market power in restricting the quantity of hops
25 available to the market from domestic production. The

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1 actions of the HAC appear to have developed an orderly
2 marketing program for hops. The degree of price
3 variability during the life of the present order has
4 been less than half that experienced otherwise.' As a
5 final indicator of the stability of the federal
6 marketing order can bring to the US hop industry, the
7 historical price and production data for US hops from
8 1965 through 2002 are presented in Appendix Table A1.
9 The price data from 1966 through 1985 when the Marketing
10 Order 991 was in effect indicates that the average price
11 of hops increased or remained stable in a fairly regular
12 pattern indicating an orderly marketing situation.
13 Starting in 1986 to the present after the order was
14 terminated, the average price of hops has increased and
15 decreased in a rollercoaster pattern. Such price swings
16 are not indicative of an orderly marketing situation and
17 often leads to a misallocation of resources. A final
18 document to support a marketing order for US hops is a
19 letter to the USDA which I wrote in 1981. This letter
20 supported the concept of the existing federal order and
21 predicted the consequences of the order's termination.
22 All of my predictions came true. In addition, I gave an
23 estimate of the impact of the last federal order had on
24 the price of beer and malted beverages in the US. It
25 was so diminutive that a consumer would not know that a

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1 federal marketing order was successful in creating an
2 orderly marketing situation. Overall, I fully support
3 the implementation of a federal marketing order with a
4 producer allotment program for the US hop industry. The
5 industry currently faces an inelastic demand and supply
6 with resulting wide price variations. It has been
7 demonstrated in the past that they, US hop producers, do
8 not unduly restrict the flow of hops to the market when
9 allowed to have some market power through a producer
10 allotment provision in a federal marketing order. US
11 hop producers are in need of such a marketing tool and
12 the countervailing power it can create for the producer
13 side of the market. If the US hop producers are not
14 allowed to use such a marketing tool, the industry will
15 continue to shrink in size and will someday become
16 extinct."

17 ***

18 BY MR. MONAHAN:

19 Q. Thank you, Dr. Folwell. To those of us
20 here who don't use terms like price flexibility
21 coefficient in everyday conversation, can you explain in
22 laymen's terms some of the more scientific or economic
23 concepts that were discussed in your report?

24 A. Basically, when economists are talking
25 about price flexibility, it's the reciprocal of the

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1 elasticity of demand with respect to price or the supply
2 elasticity. We use the term elasticity and we talk
3 about an inelastic demand for a product here, what we're
4 basically indicating is that a small change in the
5 quantity supplied or demanded can lead to very large
6 price swings as was indicated when we had the crop
7 failure in the Hallertau region of Europe back in 1979.

8 Q. That's the situation you described where
9 the price of hops had a major fluctuation.

10 A. Correct.

11 Q. What was that fluctuation?

12 A. From 75 cents a pound to \$6 a pound. I
13 used to say to my students it went from six bits to six
14 bucks overnight.

15 Q. And that's for the price of raw hops?

16 A. That's right.

17 Q. Even given that six bits to six bucks
18 swing, are you aware of whether that price fluctuation
19 resulted in any difference in the hopping of beer by
20 producers?

21 A. The hopping ratio, you're referring to?

22 Q. Hopping ratio, yeah.

23 A. Not that I'm aware of.

24 Q. Which is to say did the price change
25 affect the amount of hops that were purchased and used

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1 by the brewers?

2 A. I'm not aware of that.

3 Q. On page two of your report, you state
4 that a federal marketing order will help achieve greater
5 stability of hop farm income. Can you just describe in
6 laymen's terms, sir, how the federal marketing order
7 will accomplish that, will stabilize hop farm income?

8 A. Well basically, hops have traditionally
9 been marketed under multiple year contracts at fixed
10 prices. Just about the only agricultural commodity
11 marketed that way. Given these marketing arrangements,
12 basically a producer knows what price they're going to
13 receive for their production in the future, however, the
14 income, again, is going to be influenced by weather
15 patterns that might occur in variations and yields, but
16 it creates greater certainty as to what the farm income
17 will be from hop production.

18 Q. There's been some discussion about
19 contracting for hops. Was the use of forward contracts
20 in the old order -- was there a prevalent practice?

21 A. Yes.

22 Q. Were most hops contracted for under the
23 old order?

24 A. I think as we approached harvest each
25 year under the old federal order, the amount of hops

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1 that was contracted would usually approach 90 percent.

2 Q. Okay, do you know if that changed in the
3 aftermath of the hop marketing order?

4 A. Yes, it has.

5 Q. How did it change?

6 A. It's declined.

7 Q. Do you know -- do you have an opinion as
8 to why?

9 A. Basically, I believe that the buyers of
10 hops saw an opportunity to not enter into these long-
11 term contracts at fixed prices and take advantages of
12 lower prices.

13 Q. Do you have an opinion as to whether a
14 new hop marketing order would affect the use or
15 prevalence of forward contracts?

16 A. Basically, if I would sort of extrapolate
17 from the old marketing order, contracting was still
18 prevalent, very common, and I think it would continue
19 under a new market order.

20 Q. Sir, I see a large bound volume sitting
21 to your left on the table, about an inch, inch and a
22 quarter thick. Can you tell us what that is?

23 A. This is the dissertation that was done by
24 Mr. Habuki at Washington State University. It was an
25 econometric model of the structural supply and demand

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1 components that the US hop industry faced. It also
2 incorporated international trade flows within it.

3 Q. That's the Habuki report that you
4 reference in your report, sir?

5 A. Correct.

6 ***

7 MR. MONAHAN: I'm not going to call for that
8 as an exhibit, Your Honor, but I would like to perhaps
9 make that available if persons wanted to review it
10 during a break.

11 ADMINISTRATIVE LAW JUDGE: All right. Just
12 for the record, it's a bound volume and it's multi-
13 pages. Doctor, how would you describe how much is
14 there?

15 DR. FOLWELL: I'm not quite sure by how much
16 of what...

17 ADMINISTRATIVE LAW JUDGE: What's the last
18 page number?

19 DR. FOLWELL: 273.

20 ADMINISTRATIVE LAW JUDGE: All right. And the
21 book is roughly an inch and a quarter thick, I think.

22 DR. FOLWELL: Right. It's a bound
23 dissertation from Mr. Habuki's Ph.D.

24 ADMINISTRATIVE LAW JUDGE: What is the date of
25 the publication?

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1 DR. FOLWELL: 1984.

2 ADMINISTRATIVE LAW JUDGE: All right. Thank
3 you.

4 MR. MONAHAN: Your Honor, perhaps someone
5 could ask that official notice be taken of it?

6 ADMINISTRATIVE LAW JUDGE: Would you read into
7 the record, Dr. Folwell, the Library of Congress number
8 and so on?

9 DR. FOLWELL: There will not be a Library of
10 Congress number on this yet. This is my department's
11 copy of the dissertation which we keep in our reference
12 room. It's available from the microfilm service of the
13 University of Michigan.

14 MR. MONAHAN: Are there any other identifying
15 characteristics on the volume, sir?

16 DR. FOLWELL: The title, of course, is "United
17 States Hop Industry: Structural Analysis and Forecasts."
18 And the student's full name, first name was
19 Y-o-s-h-i-n-o-b-u, last name Habuki, is H-a-b-u-k-i.

20 MR. MONAHAN: I would ask that this court take
21 judicial notice of the publication.

22 ADMINISTRATIVE LAW JUDGE: Would you hand it
23 to me, Dr. Folwell? Let me see if I can identify it in
24 any further way. I'm reluctant to take official notice
25 of it. It is a dissertation submitted in partial

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1 fulfillment of the requirements for the degree of Doctor
2 of Philosophy. It is not -- it is a treatise that has
3 been relied upon by this witness for his testimony. I'm
4 not sure it is information that is widely relied upon by
5 professionals in the field of agricultural economics,
6 but I would entertain further testimony about that. Mr.
7 Carswell?

8 MR. CARSWELL: Your Honor, is this
9 dissertation published? Is it -- is there a publisher
10 where we could get a copy of it or is it just available
11 in this version and then on microfilm at Michigan?

12 ADMINISTRATIVE LAW JUDGE: Dr. Folwell, would
13 you answer that question for me, please?

14 DR. FOLWELL: It would be available at the
15 University of Michigan microfilm.

16 ADMINISTRATIVE LAW JUDGE: And to your
17 knowledge is it published by any publisher?

18 DR. FOLWELL: Not that I'm aware of.

19 ADMINISTRATIVE LAW JUDGE: I think it could be
20 cited in argument and it could be cited in testimony as
21 it has been, but I'm reluctant to take official notice
22 of the entire volume unless I have additional testimony
23 about the numbers of people that rely on this opinion.

24 MR. MONAHAN: Thank you, Your Honor. We just
25 want to make sure it's available to the opponents to

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1 review and understand the resources that Dr. Folwell
2 considered and relied upon in his report.

3 ADMINISTRATIVE LAW JUDGE: Yes, and I
4 appreciate that. Thank you.

5 MR. MONAHAN: Your Honor, with that, the
6 proponents have no further questions for Dr. Folwell.

7 ADMINISTRATIVE LAW JUDGE: All right, thank
8 you. I would now invite additional questions of Dr.
9 Folwell. I'd begin with those who are here in favor of
10 the proposals...

11 MR. MONAHAN: Your Honor...

12 ADMINISTRATIVE LAW JUDGE: Mr. Monahan?

13 MR. MONAHAN: ...I jumped the gun. I would
14 move for the admission of Exhibits 26 through 29.

15 ADMINISTRATIVE LAW JUDGE: Would anyone like
16 to voir dire Dr. Folwell with regard to any of those
17 exhibits? Mr. Moody, you may voir dire.

18 MR. MOODY: Well, we haven't seen 27, 28, and
19 29 yet, so I'd like to reserve on those until we've had
20 a chance to review them.

21 ADMINISTRATIVE LAW JUDGE: Good point. They
22 won't be easy to reproduce. What are your plans in that
23 regard, Mr. Monahan?

24 MR. MONAHAN: To rely upon the expertise of my
25 support staff over the lunch hour.

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1 ADMINISTRATIVE LAW JUDGE: All right. Perhaps
2 by this afternoon. Dr. Folwell, are you available all
3 day here today?

4 DR. FOLWELL: Yes, ma'am.

5 ADMINISTRATIVE LAW JUDGE: Good. Will you be
6 available other days this week?

7 DR. FOLWELL: I have to be in Walla Walla
8 tomorrow afternoon for an asparagus meeting.

9 ADMINISTRATIVE LAW JUDGE: Okay. So I think
10 today's the day. So if you can do that during the lunch
11 hour, that would be good, Mr. Monahan. All right. Let
12 me just start with Exhibit 26. Would anyone like to
13 voir dire Dr. Folwell with regard to that exhibit? Is
14 there any objection to Exhibit 26 being admitted into
15 evidence? There being none, Exhibit 26 is hereby
16 admitted. With regard to 27, 28, and 29, I'll reserve
17 ruling. All right now, questions for Dr. Folwell. I
18 would like to begin, please, with those who are here in
19 favor of the proposals. All right. I would now open
20 the floor to questions from those who are here in a
21 position against the proposals. Yes. Please identify
22 yourself for the record?

23 DR. TWEETEN: Luther Tweeten. I would like to
24 ask Dr. Folwell, on page five, to look at his price
25 elasticities demand. As I understand it, it's $-.71456$.

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1 Is that statistically different from one?

2 DR. FOLWELL: I did not run that hypothesis.

3 DR. TWEETEN: You can do a quick examination.
4 Your standard error, according to the t-value would be
5 about .36, is that correct?

6 DR. FOLWELL: Right.

7 DR. TWEETEN: The difference between one and
8 .71456 is roughly equal to that. That means your t-
9 value is approximately one that is not different from
10 zero, statistically. That means that your estimate does
11 not differ statistically from Mark Jekanowski's
12 estimate, is that correct?

13 DR. FOLWELL: I don't have his estimate in
14 front of me at this time...

15 DR. TWEETEN: Well, just unitary. That means
16 your estimate is not statistically different from
17 unitary.

18 DR. FOLWELL: But it's in the inelastic range.

19 DR. TWEETEN: No. Unitary is not inelastic.

20 DR. FOLWELL: I understand what you're saying.
21 That's -1.0. With the estimate here that we have is a
22 -.7.

23 DR. TWEETEN: But there's a high probability.

24 DR. FOLWELL: There is some probability...

25 DR. TWEETEN: There's a high probability that

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1 it doesn't differ from one.

2 DR. FOLWELL: I'll admit that there's some
3 probability.

4 DR. TWEETEN: Thank you.

5 ADMINISTRATIVE LAW JUDGE: Thank you, Dr.
6 Tweeten. Other questions for Dr. Folwell? Dr.
7 Jekanowski?

8 DR. JEKANOWSKI: Thank you, Your Honor. Dr.
9 Folwell, I'm a little bit curious about your dummy
10 variables, your D -- D1, D2, D3. Can you give a -- go
11 through a little bit more explanation about how you
12 chose those years and whether -- the decision of the
13 years to choose for dummy variables might affect the
14 results.

15 DR. FOLWELL: It definitely could, but my
16 analysis, at least in the graphical presentation of the
17 data from your report, which appears on page eight, is
18 based primarily upon a classical journal article that
19 E.J. Working [ph] wrote as what those statistical supply
20 and demand curves show, and he, basically, in that
21 article talked about the shifting supply and demand
22 curves over time and if you look at those clusters I
23 identified earlier, there's definitely years that are
24 contiguous to one another within those clusters and it
25 appears that the demand curve has been more stable than

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1 the supply curve within each cluster.

2 ADMINISTRATIVE LAW JUDGE: Dr. Jekanowski,
3 your voice projects really well, so you don't need to
4 hold it quite as close. It's fine, but just so that you
5 and the Doctor are about on the same audible level.

6 DR. JEKANOWSKI: Sure. But do you have any
7 explanation about what's going on? Why are those
8 clusters where they are? Can you explain -- you
9 mentioned that shifting demand and shifting supply,
10 what's actually changing in those years?

11 DR. FOLWELL: Well, if I were to provide my
12 opinion as to what was happening in those years, in the
13 years of 1977 through '79 in there, when you're looking
14 at those, those were pre-Hallertau crop failure years.
15 If you move up then, into the 1980s and later on there,
16 you'll notice that the demand curve is shift upwards and
17 that's basically from 1980 through 1985 is when the hop
18 market was in a -- almost a little bit of disarray
19 because the price of hops was bid up from 75 cents a
20 pound to \$6 a pound. Then after realizing that that
21 level of hop and the hops that were contracted were no
22 longer necessary. The price started dropping back down
23 and the demand curve shifted down. And that can be well
24 demonstrated by some actions that were taken by dealers
25 in the market. There were actually contracts signed to

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1 raise hops by farmers who were not hop growers at the
2 time, back in '79 and '80, and hop dealers had to go
3 back and buy those contracts back. They overbid the
4 price of hops.

5 DR. JEKANOWSKI: So -- but just to clarify.
6 Those years that you chose are really just a function of
7 what you see in this scatter plot. There's no
8 fundamental explanation from an economic standpoint as
9 to why you would include those years.

10 DR. FOLWELL: I thought I just offered a very
11 good one in the sense of what happened -- from previous
12 to '79, the overreaction in the hop industry in that
13 upwards cluster in there and then the backing off or the
14 shifting to the left of the demand curve. And this type
15 of analysis is well documented in classical journal
16 articles. Matter of fact, I have my students always
17 make a graph before they start fitting equations.

18 DR. JEKANOWSKI: What would happen if you
19 included beer production in your equation?

20 DR. FOLWELL: I'd have to rerun the equation.

21 DR. JEKANOWSKI: Could it change the results?

22 DR. FOLWELL: Any time you introduce another
23 variable in there all of the coefficients, the values of
24 them will change slightly.

25 DR. JEKANOWSKI: So could it be possible that

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1 there's [sic] some variables in there that you should've
2 included but did not?

3 DR. FOLWELL: Basically, I believe you had the
4 Log of Beer Production in your model and it was not
5 statistically significant.

6 DR. JEKANOWSKI: Well...

7 DR. FOLWELL: And I duplicated your results.

8 DR. JEKANOWSKI: Okay. Well, this sort of --
9 for the record here. In most of the classes I took --
10 or that I ever took, I was always taught that
11 insignificance, alone, isn't a reason for excluding a
12 variable.

13 DR. FOLWELL: That depends upon all of the
14 other statistical problems you might face, including
15 multi-collinearity [ph].

16 DR. JEKANOWSKI: That's all -- that's all it
17 depends on?

18 DR. FOLWELL: No. But that's one reason for
19 an inclusion of a non-significant variable. You could
20 have also have knowledge of the industry, that in fact,
21 this variable is so highly important that it has to be
22 included in there. It could be that in a large
23 simultaneous supply and demand model that you found out
24 that beer production impacts other components of supply
25 and demand.

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1 DR. JEKANOWSKI: Sure. But -- so there are --
2 there could be good reasons for including it in there.

3 DR. FOLWELL: That's not my preference, as a
4 researcher.

5 DR. JEKANOWSKI: Okay. You made reference in
6 your document to the near perfect substitution of German
7 hops for US hops, is that right?

8 DR. FOLWELL: For the same variety that's
9 processed or handled in the same manner with same level
10 of alpha, yes.

11 DR. JEKANOWSKI: So what would happen, in your
12 opinion, if we were to restrict supply of the US hops
13 given that there is a perfect substitute, or a near
14 perfect substitute that's not restricted?

15 DR. FOLWELL: Well, basically, the dealers or
16 the buyers could turn to hops from Europe or other
17 producing areas in the world. There have been occasions
18 in the past when the hop industry has turned to imported
19 hops, primarily from China, which we labeled as food
20 grade vegetative matter in some -- other research we did
21 on hops at WSU. They had such low capacity for brewing
22 or imparting any type of flavoring to it that they were
23 actually blended with hops from the US. They were
24 imported at 25 cents a pound.

25 DR. JEKANOWSKI: Would you agree that,

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1 generally speaking, technology is transferable across
2 international borders, as well as hops?

3 DR. FOLWELL: Yes.

4 DR. JEKANOWSKI: So at least, hypothetically,
5 Chinese growers could start producing high quality, high
6 alpha hops?

7 DR. FOLWELL: Hypothetically, yes. In
8 reality, I doubt it.

9 DR. JEKANOWSKI: Can you expand on that?

10 DR. FOLWELL: I doubt it, because I don't
11 think they necessarily have the knowledge, the
12 background, or the support to do it in terms of massive
13 research programs which support this industry here.

14 DR. JEKANOWSKI: Just as sort of an aside --
15 and I understand. I mean, you might not follow this
16 industry, but I want to do sort of an analogy here. Say
17 15 or 20 years ago, did most US soy bean producers
18 expect Brazil or Argentina to one day be the world's
19 largest producer of soy beans?

20 DR. FOLWELL: No, sir.

21 DR. JEKANOWSKI: What happened? How come they
22 are today?

23 DR. FOLWELL: I can't really explain about soy
24 beans. I could tell you about a few other crops, such
25 as asparagus or things of that nature.

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1 DR. JEKANOWSKI: So certainly, overseas
2 producers have the capacity to invest in technologies
3 and to increase production far beyond what they -- the
4 situation is currently?

5 DR. FOLWELL: Usually, the environment
6 overseas is completely different than what it is here in
7 the US in terms of producing a comparable product.
8 Typically, the cost of inputs are significantly
9 different. Usually, labor is much cheaper. They
10 substitute a lot of labor for technology, where here in
11 the United States, I think in terms of agriculture, you
12 see the substitution of technology for labor.

13 DR. JEKANOWSKI: Sure, that's right now. But
14 still, hypothetically, it's not out of the realm of
15 possibility for China to become a major producer of hops
16 in the future given that technology is transferable, is
17 that correct?

18 DR. FOLWELL: Well, they might become a major
19 producer of hops, but currently -- and not dealing with
20 a hypothetical, they produce a very low quality hop.

21 DR. JEKANOWSKI: Now, if the world market
22 price for hops increased, would that increase the -- how
23 would that affect the incentive for China to invest in
24 technologies to increase their production?

25 DR. FOLWELL: I would assume it would give

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1 them a positive indicator that they should invest, but
2 whether they do or not, I can't answer that question.

3 DR. JEKANOWSKI: No, but it -- I think it
4 would -- all else equal, it would increase their...

5 DR. FOLWELL: Hypothetically, yes.

6 DR. JEKANOWSKI: Hypothetically, sure. How
7 about Germany? If the world price of hops increased,
8 would they decrease production or increase?

9 DR. FOLWELL: Germany's an interesting
10 situation, because at least when I was following the hop
11 industry closely, they actually had a grubbing policy
12 for taking hops out. So I'm not sure if they would or
13 not.

14 DR. JEKANOWSKI: So if the world price
15 increased, they still might take more hops out, you're
16 thinking?

17 DR. FOLWELL: Not -- well, they could. They
18 could also increase it. It depends upon the policies of
19 their government and the European Union.

20 DR. JEKANOWSKI: And so what would happen to
21 price if, hypothetically, a reduction in US supply,
22 because of the marketing order, was met with an equal or
23 greater increase in production in Germany or China?

24 DR. FOLWELL: Wouldn't the price remain the
25 same? If it was offset with production in other

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1 countries?

2 DR. JEKANOWSKI: I don't -- I mean, that's why
3 I'm asking you. It would, right?

4 DR. FOLWELL: Well, I'm asking you back.
5 That's probably what would happen.

6 DR. JEKANOWSKI: And so, to sort of come right
7 back, is there any fundamental reason to believe that
8 production would not increase overseas with a -- if we
9 imposed a supply restriction in the US?

10 DR. FOLWELL: It's possible, but you also have
11 to stop and realize the major capital investments that
12 are needed to produce quality hops. And most of the
13 agricultural production in other countries which I'm
14 familiar with, you do not see that amount of capital
15 investment taking place.

16 DR. JEKANOWSKI: But it is possible to get
17 that capital investment?

18 DR. FOLWELL: Perhaps.

19 DR. JEKANOWSKI: Okay. I noticed in other
20 parts of your testimony, you made reference to the -- I
21 forget how it was phrased -- lack of competitive
22 position, or competition in the market for hops,
23 implying that maybe there was market power being
24 exercised or something to that effect driving prices
25 lower. Is that roughly paraphrasing correct?

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1 DR. FOLWELL: Well, I think that when you have
2 only basically three or four buyers of hops versus a
3 number of independent producers out here that the market
4 power's going to be on the side of the buyers.

5 DR. JEKANOWSKI: In your understanding, are
6 aroma hops in equilibrium, in balance?

7 DR. FOLWELL: I really haven't looked at the
8 statistics on that. I assume that the major buyer of
9 the aroma hops would probably say it is right now.

10 DR. JEKANOWSKI: Well, just -- since you
11 didn't have the benefit of testimony last week, it did
12 sort of come out over and over again that -- I think
13 there seems to be a general agreement that the problem
14 was not in aroma hops, it was in alpha hops. So given
15 that, can you explain is there a -- what's the
16 difference in the competitive position of buyers in the
17 aroma hop -- you know, aroma hops versus hops. That
18 justifies the need for a marketing order?

19 DR. FOLWELL: Well, basically, the marketing
20 order with the producer allotment provision, which
21 they're asking for, is to provide an orderly flow of
22 hops of the market. There's been a tendency in this
23 industry because of the price swings, the price cycles
24 that occurred, that any slight increase in price leads
25 to almost an over response in terms of the amount of hop

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1 yards that are put back into production. I've watched
2 this industry go from 50 some thousand acres of hops
3 down to -- into the low 30s, I believe right now, in
4 terms of their acreages and right now there's hop yards
5 around here that are laying idle. Those resources have
6 very little salvage value in terms of alternative uses.
7 Those poles out there and the wire -- the poles are
8 basically good for fire wood and the wire you can take
9 to the junkyard. So if they can utilize them in hop
10 production, they're going to attempt to do it.

11 DR. JEKANOWSKI: Utilize the land, you mean?

12 DR. FOLWELL: Um-hum.

13 DR. JEKANOWSKI: All right. So you just said
14 that for a small change in price, there's a dramatic
15 change in supply?

16 DR. FOLWELL: There has been in recent years.

17 DR. JEKANOWSKI: And does that also apply to
18 foreign producers?

19 DR. FOLWELL: I can't -- I have no knowledge
20 of that.

21 DR. JEKANOWSKI: Okay. Let's see. In your
22 opinion, or maybe in your experience, modeling the hop
23 sector and setting the saleable and whatnot, how did you
24 predict German crop failures?

25 DR. FOLWELL: I never predicted a crop

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1 failure. If I could do that, I wouldn't be sitting here
2 doing this, if I could predict the weather and diseases
3 and insects. The crop failure that occurred in the
4 Hallertau region, to be honest with you, I don't recall
5 what, exactly, the reason was or whether it was weather-
6 related, or some other cultural aspect entered into the
7 problem over there that year. But if there is a
8 failure, it tends to be some type of disease-related,
9 insect-related, or it could be weather, at times.

10 DR. JEKANOWSKI: Is that a concern at all as
11 -- for a committee to be basically dictating the supply
12 conditions in the US? The inability to control for
13 failures -- over crop failures in the US or overseas?

14 DR. FOLWELL: The statistical committee, which
15 I think you're probably making reference to here,
16 basically did not put into any of their projections any
17 possible crop failures or anything of that nature. If
18 they knew there were problems in terms of producing the
19 hops in terms of some disease or something and there was
20 no possible control for it, then yes, I mean, that would
21 affect the trends that they're looking at, anyway.

22 DR. JEKANOWSKI: It would also affect the
23 market equilibrium even after all of the effort by the
24 committee.

25 DR. FOLWELL: If there's a crop failure, it's

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1 going to impact price, yes.

2 DR. JEKANOWSKI: And if the committee's
3 working as planned, assuming that it's restricting
4 supply to some degree, to raise prices or stabilize
5 prices, or whatever, would that not -- would then a
6 German crop failure amplify the effect on prices?

7 DR. FOLWELL: Well, first of all, my research
8 indicated that they did not unduly restrict the flow of
9 hops to the market and second of all, yes, if there's a
10 crop failure then, you know, the price is going to move
11 up in a very rapid fashion.

12 DR. JEKANOWSKI: Have you done any, you know,
13 thinking in the process of putting this testimony
14 together -- have you done any thinking about what the
15 saleable would have to be currently? Under this --
16 under the proposed order?

17 DR. FOLWELL: No, I haven't. I actually have,
18 I believe, a copy here of the balance sheet that we used
19 on the HAC. We'd have to go through and make
20 projections here as much as 18 months into the future
21 and then calculate what the saleable would be based upon
22 whatever the 100 percent of the saleable would be set by
23 this new order, so it's -- it's impossible to do. I can
24 show you the accounting formulas or the balance sheet
25 approach they used here, but not knowing what the base

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1 is -- 100 percent of the base -- how can you calculate a
2 saleable percentage, even if you make projections as to
3 supply and demand components? I think it's impossible.

4 DR. JEKANOWSKI: But you can come up with some
5 idea of what the initial base would be, can't you?
6 Based on this proposal?

7 DR. FOLWELL: I assume that the -- that
8 through this hearing process and working with the USDA,
9 that they will set what 100 percent of the saleable will
10 be, at least in terms of pounds. From there on out, no,
11 I can't right now.

12 DR. JEKANOWSKI: But -- all right, do you at
13 least know that the base is going to be vastly inflated
14 from, say, current production levels of alpha?

15 DR. FOLWELL: I don't know that, personally.

16 ADMINISTRATIVE LAW JUDGE: Dr. Jekanowski, why
17 don't you lay out a hypothetical that if the base was
18 calculated thus and so...

19 DR. JEKANOWSKI: Sure, okay. Yeah. And I'll
20 cover some of this in my testimony so we probably don't
21 need to get too detailed. But the way your proposal is
22 written...

23 ADMINISTRATIVE LAW JUDGE: Not quite so close
24 to the mike.

25 DR. JEKANOWSKI: Oh, I'm sorry. Is this okay?

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1 ADMINISTRATIVE LAW JUDGE: Yes.

2 DR. JEKANOWSKI: Okay. The way the proposal's
3 written, each grower chooses their highest production
4 over the past five or six years. Does that bear on a
5 personal base? That's correct, right? It...

6 DR. FOLWELL: Is this a hypothetical...

7 DR. JEKANOWSKI: No, this is real. I mean,
8 this is...

9 DR. FOLWELL: If you say it's in the proposal,
10 then I assume that it's the...

11 DR. JEKANOWSKI: So you haven't actually --
12 have you studied the proposal?

13 DR. FOLWELL: Not in any great detail.

14 DR. JEKANOWSKI: So you don't necessarily know
15 how this proposal's going to work?

16 DR. FOLWELL: In general, I do.

17 DR. JEKANOWSKI: Okay. All right, well --
18 then just to finish with this hypothetical. If every
19 producer picks their highest production period over the
20 past five years and any hop grown over the past five
21 years that has an alpha acid level of less than 10
22 percent is granted 10 percent alpha, those two
23 conditions combined inflate the base, is that correct?
24 This -- I mean, no producer would ever pick his own past
25 five year production period that's less than the maximum

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1 production.

2 DR. FOLWELL: Correct.

3 DR. JEKANOWSKI: Correct, okay. Okay, are you
4 following -- do you agree that the base is going to be
5 vastly over-inflated? Based on those...

6 DR. FOLWELL: I think you're misinterpreting
7 what this base is and what the saleable percentage is
8 and everything. It says if somebody's out here to
9 inflate this base and then unduly restrict the flow of
10 hops, personally, from an economist's point of view, I
11 don't care whether the saleable is 200 percent or 50
12 percent, as long as the administrative committee of the
13 order is allowing an adequate volume of hops or alpha
14 acid flow to the market. I think it's immaterial what
15 the saleable percentage is.

16 DR. JEKANOWSKI: But isn't it material for
17 individual producers -- that wealth is transferred
18 between producers?

19 DR. FOLWELL: In terms of the transferability
20 of base, which you're getting into now, I have a whole
21 theory upon that and how that can be corrected and
22 furthermore, I don't think the USDA basically wants the
23 value of such a marketing program to be embedded in the
24 base.

25 DR. JEKANOWSKI: So in your opinion, is there

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1 going to be a value for base on this...

2 DR. FOLWELL: If the order is successful, as
3 any farm program, if it's successful, the value of that
4 program will be embedded in some resource which the
5 grower has control of. In wheat and corn and soy beans,
6 it's land. Here, it happens to be in a transferable
7 base.

8 DR. JEKANOWSKI: So the full benefits of the
9 program will be capitalized into the value of the base?

10 DR. FOLWELL: If the program is successful,
11 there will be some value capitalized into the base.

12 DR. JEKANOWSKI: And who benefits from that?

13 DR. FOLWELL: Now? Nobody. There's -- I
14 mean, this doesn't exist. Hypothetically, if this were
15 to come about, what I would suggest to the
16 administrative committee, and they were about ready to
17 shoot me about 17 years ago for supporting or even
18 suggesting this idea, was that there's going to be some
19 office work or paper work necessary to keep track of
20 this -- of these transfers as they occur, that that
21 money, to cover those costs, go to the administrative
22 committee, that the remainder of it go to the US
23 Treasury to offset the federal deficit, because it was
24 the beer drinkers of America from which it came.

25 DR. JEKANOWSKI: All right, you lost me here.

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1 Okay, where did the federal treasury come into this?

2 DR. FOLWELL: Pardon me?

3 DR. JEKANOWSKI: You completely lost me.

4 DR. FOLWELL: Okay. If there's a value to
5 this base and everything, then it has to be -- somehow,
6 this price of hops must be "higher" than what somebody
7 expected, right?

8 DR. JEKANOWSKI: I'm asking the questions now.
9 Technically, you're on the stand, I'm asking questions.

10 DR. FOLWELL: If that occurs, then somehow --
11 and I think I estimated in a letter to the USDA once,
12 that the price, the average price of a 12 ounce can or
13 bottle of beer was increased by .0000085 cents per 12
14 ounce container. Okay. Somehow, that money, then, is
15 associated with the value of this base. If that base
16 has value, and if one grower wants to transfer it to
17 another grower for many reasons, diseases, fires, et
18 cetera, reasons they can't grow hops, then the cost of
19 keeping track of that base, the cost of it, the grower
20 should pay to the administrative committee anything in
21 excess of the cost of keeping track of that base, as far
22 as I'm concerned, should be given back to the federal
23 government and used to reduce the federal deficit.

24 DR. JEKANOWSKI: Sir, is this part of the
25 original proposal? Is this...

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1 DR. FOLWELL: No, that was...

2 DR. JEKANOWSKI: ...something that we can
3 question about, or...

4 DR. FOLWELL: That was mine when they wanted
5 to shoot me once. They -- you know, the idea of giving
6 back to the government some money just wasn't very
7 appealing, but in fact, it's the most equitable way I
8 know of returning the money to society.

9 DR. JEKANOWSKI: So in your opinion,
10 currently, there -- the money is not equitably
11 distributed?

12 DR. FOLWELL: Giving back to society?

13 DR. JEKANOWSKI: Yeah.

14 DR. FOLWELL: Well, under the old order, no,
15 it wasn't.

16 DR. JEKANOWSKI: And under the proposed order?

17 DR. FOLWELL: I have no idea what's going to
18 happen under the proposed order. I have no idea if it's
19 going to be successful. I hope it is for the sake of
20 the industry, but I don't know. And I don't know what
21 the rules are going to be involving transfers. Or
22 selling of the base.

23 MR. BARTON: Can we go off the record?

24 ADMINISTRATIVE LAW JUDGE: Yes, let's go off
25 record.

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1 ***

2 [Off the Record]

3 [On the Record]

4 ***

5 ADMINISTRATIVE LAW JUDGE: All right, we're
6 back on record. We went off record at 10:42, it's still
7 10:42.

8 DR. JEKANOWSKI: Are we back -- I'm sorry, I
9 wasn't paying...

10 ADMINISTRATIVE LAW JUDGE: We're on record.

11 DR. JEKANOWSKI: Okay. Thank you. I have
12 nothing further for now, Your Honor. Thank you, Mr.
13 Folwell.

14 ADMINISTRATIVE LAW JUDGE: Thank you, Dr.
15 Jekanowski. Dr. Tweeten?

16 DR. TWEETEN: Luther Tweeten again. I just
17 wanted to go back for one additional question. On page
18 five, your equation, you're referring here in your
19 production estimate, I assume, to US production?

20 DR. FOLWELL: That's correct.

21 DR. TWEETEN: In a demand equation?

22 DR. FOLWELL: The quantities on the left hand
23 side and the prices on the right, yes.

24 DR. TWEETEN: How about international trade?

25 There are other sources of demand quantity and trade is

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1 one of them. Stocks are another. How are these
2 accounted for in your equation?

3 DR. FOLWELL: They're not accounted for. I
4 was just trying to follow the example of what Sparks put
5 forward to indicate the limitations of that equation.

6 DR. TWEETEN: If you had accounted for them,
7 what would you anticipate the effect would be on the
8 elasticity of demand?

9 DR. FOLWELL: I...

10 DR. TWEETEN: Do these add to the elasticity
11 or subtract from it?

12 DR. FOLWELL: Add or subtract, do...

13 DR. TWEETEN: Do they make the price
14 elasticity demand higher or lower? When you take into
15 account the stock demand and the international trade
16 demand.

17 DR. FOLWELL: The Habuki model, which I
18 referred to earlier, came up with an in-elastics demand,
19 which were less elastic than what I had and that the
20 econometric model did account for international trade
21 and stock demands.

22 DR. TWEETEN: But you didn't answer my
23 question, which was if you would have added that to your
24 equation, what would you anticipate? The effect would
25 based on economic theory.

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1 DR. FOLWELL: I don't believe you can take
2 into account all those relationships within a single
3 equation. I would assume that if I were allowed to
4 estimate a complete econometric model or redo the Habuki
5 model, they would come out actually probably less
6 elastic.

7 DR. TWEETEN: I might say that that's in
8 variance with all the economic theory that I'm aware of.

9 ADMINISTRATIVE LAW JUDGE: Was that a question
10 or testimony?

11 DR. TWEETEN: That's it. I'm responding to
12 his comment that...

13 ADMINISTRATIVE LAW JUDGE: Okay, so you want
14 it...

15 DR. TWEETEN: ...elasticity.

16 ADMINISTRATIVE LAW JUDGE: You want to ask
17 him, then, do you agree?

18 DR. TWEETEN: Do you agree that economic
19 theory says that when you include stock demand and
20 international trade demand, that tends to make the
21 demand elasticity greater?

22 DR. FOLWELL: In a single equation, model?

23 DR. TWEETEN: Well, any model.

24 DR. FOLWELL: Well, all I can do, Dr. Tweeten,
25 is refer to the Habuki dissertation and in fact, when we

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1 accounted for all those, his estimated elasticity was
2 less elastic than what I thought.

3 DR. TWEETEN: But was it greater when he took
4 into account just the domestic production or when he
5 took into account all?

6 DR. FOLWELL: We did not calculate that.

7 DR. TWEETEN: Thank you.

8 ADMINISTRATIVE LAW JUDGE: Thank you, Dr.
9 Tweeten. Additional questions for Dr. Folwell from
10 those who are here against the proposals? Mr. Carswell?

11 MR. CARSWELL: Dr. Folwell, Matt Carswell. A
12 significant portion of your comments, or your paper,
13 consisted of a critique of the Sparks report and forgive
14 me, I'm a layman, and I'm not sure about that exchange
15 between yourself and Dr. Tweeten, but if I'm not
16 mistaken, did I understand that the results of your
17 equation would be -- statistically insignificant from
18 the results from the Sparks study?

19 DR. FOLWELL: Would not differ significantly?

20 MR. CARSWELL: Yes, sir.

21 DR. FOLWELL: That's what Dr. Tweeten was
22 talking about in terms of the hypothesis testing.

23 MR. CARSWELL: And did you agree with that, or
24 that there was a strong probability that it would not
25 differ significantly?

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1 DR. FOLWELL: I indicated there was a
2 probability that it would not differ -- not differ.

3 MR. CARSWELL: Thank you. You mentioned
4 earlier that the Chinese hops were described as
5 something to the effect of vegetative matter, pretty low
6 quality. Is that correct?

7 DR. FOLWELL: Food-grade vegetative matter.

8 MR. CARSWELL: When was that assessment given?

9 DR. FOLWELL: After the termination of the
10 last marketing order, the industry, I believe primarily
11 through Hop Growers of America were still attempting to
12 put together market information, supply and demand
13 production prices, et cetera, in various countries and
14 when they were looking at this, basically, they could
15 not account for all of the hops that were out there in
16 the market. There was a problem in the old marketing
17 order -- we would've referred to it as a balancing item.

18 MR. CARSWELL: Thank you. That points that
19 balancing item. Thank you. Would it surprise you to
20 learn that a substantial percentage, perhaps a majority,
21 but a substantial percentage of the hops used by Chinese
22 brewers are Chinese-grown hops?

23 DR. FOLWELL: I wouldn't be surprised at that.

24 MR. CARSWELL: Have you kept up with the
25 Chinese hop industry over the last 15, 20 years?

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1 DR. FOLWELL: Not other than seeing, you know,
2 what the Hop Growers of America put in their
3 publications.

4 MR. CARSWELL: If you wouldn't mind, could you
5 identify some of the other hop growing regions around
6 the world outside the US?

7 DR. FOLWELL: Germany, Czechoslovakia, England
8 -- do you want me to just read them here or do you want
9 me to -- it's from the International Hop Growers
10 Convention, the numbers that were reported there.

11 MR. CARSWELL: That would be great.

12 DR. FOLWELL: Australia, Belgium, Bulgaria,
13 China, the Czech Republic, Germany, France, New Zealand,
14 Poland, Portugal, Russia, Slovenia, Spain, England, the
15 Ukraine, the USA -- I shouldn't have mentioned those --
16 Yugoslavia, South Africa, Austria.

17 MR. CARSWELL: Do you know, in a rough
18 approximation, what percentage of the hops per -- on a
19 pound basis, are grown in the US?

20 DR. FOLWELL: Here the estimate for 2003 was
21 approximately 54 million pounds in the US and for the
22 total for these countries, it was 239 million.

23 MR. CARSWELL: So that's somewhere south of...

24 DR. FOLWELL: 50 percent.

25 MR. CARSWELL: Somewhere south of 30 percent

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1 and maybe even...

2 DR. FOLWELL: Right.

3 MR. CARSWELL: ...25 percent?

4 DR. FOLWELL: Correct.

5 MR. CARSWELL: That's -- it's a little over 25
6 percent, I think. Yeah. And do you have any idea on
7 the percentage of alpha on an alpha basis, the
8 percentage?

9 DR. FOLWELL: No, I don't. Not off the top of
10 my head. I'd have to look it up.

11 MR. CARSWELL: Okay. You mention on page two
12 of your report that it's anticipated that the federal
13 marketing order will, and then point two, increase hop
14 prices in the long run and yet, your report also talks
15 about the near perfect substitutability of German hops.
16 Are there other hops grown in the world that are also
17 near perfect substitutes for American hops?

18 DR. FOLWELL: I would assume so, but I can't
19 name them right now.

20 MR. CARSWELL: Would, say, Saaz hops from the
21 Czech Republic be near perfect substitutes?

22 DR. FOLWELL: I have no idea.

23 MR. CARSWELL: Would rich Alsatian hops be
24 near perfect substitutes?

25 DR. FOLWELL: Do they irrigate them?

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1 MR. CARSWELL: Yes.

2 DR. FOLWELL: I have no idea.

3 MR. CARSWELL: Considering the fact that 20
4 something percent, on a pound basis -- we don't know
5 what the alpha -- we haven't established in the record
6 yet what the alpha percentage is, but considering the 20
7 something percent of the pound basis of hops are grown
8 in the US and 70 something percent are grown outside the
9 US, how would you explain why a restriction in the US
10 applied would result in increased prices in the long
11 run?

12 DR. FOLWELL: Based upon history of what
13 happened in the previous marketing order, and the fact
14 that the nominal price of hops for every year in which
15 that order was in existence either remained stable or
16 increased.

17 MR. CARSWELL: Let's go to that first table
18 that you provided us. Or first chart, I'm sorry.
19 Figure one.

20 DR. FOLWELL: Okay.

21 MR. CARSWELL: On the -- first we could look
22 at the year '77 through '79. This is during the period
23 of the hop marketing order, correct?

24 DR. FOLWELL: Correct.

25 MR. CARSWELL: And when did the prices showing

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1 there for those years, what is the range of pricing
2 there?

3 DR. FOLWELL: Oh, between -- what? About 12,
4 13, and 14. This is the price of alpha now. It's not
5 the price of hops, which I made reference to in my
6 previous answer.

7 MR. CARSWELL: Yes, sir. And then if you have
8 looked for the post-marketing years of 1986 to 1990,
9 what is the range of pricing there?

10 DR. FOLWELL: They're slightly higher for the
11 price of alpha.

12 MR. CARSWELL: Is it about \$15 per pound and
13 \$19 per pound?

14 DR. FOLWELL: Yes, sir.

15 MR. CARSWELL: As compared to somewhere below
16 \$13 a pound and \$14 a pound.

17 DR. FOLWELL: Correct.

18 MR. CARSWELL: And then if you look at the
19 years '91 through 2001, what is the range of prices?

20 DR. FOLWELL: Basically, the same as what it
21 was in the late '80s. From approximately 16 up to about
22 19.

23 MR. CARSWELL: So the prices between '86 and
24 2001 were higher than -- from the year '78 through --
25 excuse me '77 through '79.

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1 DR. FOLWELL: For the price of alpha, yes.

2 MR. CARSWELL: And so the history of the hop
3 marketing order, at least for the year '77 through '79
4 would not support higher prices for hops, is that
5 correct? Would not support your hypothesis that prices
6 will increase for hops?

7 DR. FOLWELL: Basically, if you look back at
8 the -- on page 11, the table, you'll notice that the
9 price of hops in '77, '78, '79 went from .90, .90, .98
10 then jumped up to a \$1.50 after the crop failure in the
11 Hallertau region. So -- and you can look at previous
12 years and basically, the marketing order had the effect
13 of increasing or stabilizing prices every year. This is
14 the price of hops now I'm talking about in this table,
15 not the price of alpha, which you're referring to in
16 figure one.

17 MR. CARSWELL: You just mentioned after the
18 crop failure the prices increased.

19 DR. FOLWELL: Yes.

20 MR. CARSWELL: So was it the crop failure that
21 resulted in the increased prices or was it being under
22 an HMO?

23 MS. FINN: I believe it was a crop failure,
24 because I even had a hop dealer offer me a contract to
25 raise hops and I live over in Pullman, Washington, where

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1 you don't raise hops.

2 MR. CARSWELL: So prices increased because of
3 the crop...

4 DR. FOLWELL: The crop failure.

5 MR. CARSWELL: Because of the crop failure,
6 not because of the hop marketing order?

7 DR. FOLWELL: Right.

8 MR. CARSWELL: So again how does -- figure one
9 in the information there and also your conclusion that
10 the price increases were caused by a hop [sic] failure.
11 How does that support a hypothesis that a new hop
12 marketing order would result in higher prices in the
13 long run?

14 DR. FOLWELL: This would be an objective of
15 the order. I'm not saying it's going to necessarily do
16 it. We just hope that that's an objective that's
17 achievable.

18 MR. CARSWELL: But you don't know if it's
19 achievable?

20 DR. FOLWELL: No. If I could predict that, as
21 I indicated earlier, it's like predicting the weather.
22 I wouldn't be sitting here.

23 MR. CARSWELL: Mark was mentioning the way
24 that the saleable quantity would be set and base
25 allotment, how it would be set. Do you mind if I try a

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1 hypothesis and walk through that?

2 DR. FOLWELL: Everything seems to be
3 hypothetical. Go ahead.

4 MR. CARSWELL: I appreciate that. Presume
5 that each grower can choose his best production year
6 from 1997 through 2002 and I believe you've already said
7 this and I'm sorry to retread, but I believe you said
8 that it would be economically logical that each grower
9 would choose their production as the amount that they
10 would use to set their base allotment.

11 DR. FOLWELL: Correct.

12 MR. CARSWELL: So it stands to reason that if
13 you take each grower's very best year, then that's going
14 to result in some percentage over the previous year's
15 total hop production, is that correct?

16 DR. FOLWELL: Correct.

17 MR. CARSWELL: And then if you also take into
18 account that aroma hop growers receive a bump from
19 whatever their alpha percentage is, up to 10 percent,
20 that that's also going to result in an inflation of the
21 base allotment that will be received, is that correct?

22 DR. FOLWELL: Correct.

23 MR. CARSWELL: So would you -- just take for
24 purposes of the hypothesis that this would result in a
25 40 percent increase in the allotment, base allotment

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1 from the previous year production. So we're into 140
2 percent.

3 ADMINISTRATIVE LAW JUDGE: Mr. Carswell, just
4 so I'm clear on your hypothetical, the production is the
5 production of alpha acid or is it the production of
6 pounds of hops?

7 MR. CARSWELL: Alpha acid, Your Honor. Thank
8 you.

9 ADMINISTRATIVE LAW JUDGE: All right. Go
10 ahead.

11 MR. CARSWELL: So that the saleable quantity
12 -- well, if that were the case, so we're at 140 percent,
13 how much would you estimate the saleable quantity? How
14 much would it need to be cut just to get production at
15 some minimal level below current production?

16 DR. FOLWELL: Well, something less than 140,
17 but as I indicated earlier, to me, it's immaterial
18 whether the saleable percentage is at 200 percent or 50
19 percent.

20 MR. CARSWELL: Well, I'll try to...

21 DR. FOLWELL: Without restricting the flow of
22 alpha acid to the market.

23 MR. CARSWELL: Yes, sir, I'll try to explain
24 the materiality in a minute, but if we could just take
25 it a step at a time, that would be -- I'd appreciate it,

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1 Dr. Folwell.

2 DR. FOLWELL: Um-hum.

3 MR. CARSWELL: How much of a percent in the
4 cut of saleable quantity would you foresee for there to
5 be a reduction in the amount of hops sold in the US?
6 From US producers?

7 DR. FOLWELL: To reduce the amount of alpha
8 acid...

9 MR. CARSWELL: Yes, acid...

10 DR. FOLWELL: ...it would be something less
11 than 140 percent, but you know, exactly would depend
12 upon the projections of the administrative committee and
13 what their philosophy was about trying to capture a
14 larger share of the market.

15 MR. CARSWELL: Right. And you have to look
16 into the future, but just to get below the previous year
17 production, you would need to be somewhere in excess of
18 40 percent, correct?

19 DR. FOLWELL: Of the previous year -- of the
20 highest year, you mean?

21 MR. CARSWELL: No. The cut from the base
22 allotment, which we presumed is 140 percent of the
23 previous year, you would need a cut of somewhere north
24 of 40 percent to achieve a reduction in the amount of
25 hops sold in the US.

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1 DR. FOLWELL: If they were attempting to
2 restrict the flow of hops, yes, but...

3 MR. CARSWELL: Yes. So if they wanted to cut
4 production, which I understand is kind of the basic idea
5 here, isn't it? To cut production to increase prices
6 over the long run?

7 DR. FOLWELL: I believe, under the enabling
8 legislation, it's against the law to try and control
9 production.

10 MR. CARSWELL: So you don't think that they'll
11 have the authority to control production?

12 DR. FOLWELL: They can influence the supplier
13 response, but they cannot control production.

14 MR. CARSWELL: You don't think the way the hop
15 marketing order would work would be -- give them the
16 ability to control production by setting the saleable
17 quantity?

18 DR. FOLWELL: I think it influences a supplier
19 response, but I think every grower out there, both a hop
20 grower and non-hop growers would still be free to plant
21 as many acres as they wanted to hops.

22 MR. CARSWELL: Okay. And you're absolutely
23 right, but would they -- would it be able -- would it
24 enable the control of the sale of hops?

25 DR. FOLWELL: That's what the allotment is

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1 about is to create an orderly flow to the market.

2 MR. CARSWELL: And is it the idea to increase
3 prices, you would have to restrict the amount of hops
4 sold, wouldn't it? Wouldn't you?

5 DR. FOLWELL: With everything else held
6 constant, yes.

7 MR. CARSWELL: Yes. Yes, sir. Now, I'm going
8 to give you a little more of the hypothetical. So we're
9 presuming that you would cut it somewhere in excess of
10 40 percent just to achieve a restriction in the amount
11 of hops sold. That's -- we're on the same page?

12 DR. FOLWELL: Is that a statement or a
13 question?

14 MR. CARSWELL: Question.

15 DR. FOLWELL: Question? We can start there.

16 MR. CARSWELL: Okay. Now, if you could take
17 grower A, who has had expanding production between '97
18 and 2002, so that his -- and he hopes to keep his
19 production at least steady, and you have grower B, who
20 has had declining production from '97 to 2002, grower A
21 -- well, grower B would have -- if he -- if grower B is
22 not planning to increase his production, but is planning
23 to stay at his reduced level, grower B is going to have
24 base allotment to sell. Is that accurate?

25 DR. FOLWELL: Depending upon the saleable.

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1 MR. CARSWELL: And grower A -- if we could
2 assume, for purposes of this hypothesis that 50 percent
3 reduction in the saleable quantity from the base, so
4 that would reduce from the previous year around 10
5 percent. Grower A would need -- if he wanted to
6 maintain his supply, he would need to buy base, is that
7 correct?

8 DR. FOLWELL: I think that would depend upon
9 how the initial base is allocated under a possible new
10 marketing order. If they each can pick their highest
11 year...

12 MR. CARSWELL: Um-hum.

13 DR. FOLWELL: ...what you're talking about --
14 if he picked the highest year, being the last year of
15 2003 or 2002, I can't remember what you said there and
16 if the saleable was set below 100 percent, then
17 possibly, yes.

18 MR. CARSWELL: So if -- yeah. If his highest
19 year was 2002 and so he received a base for that amount
20 and the saleable quantity was cut by 50 percent, it
21 would seem that he would need to acquire a base, is
22 that...

23 DR. FOLWELL: If he was going to market the
24 same volume of hops.

25 MR. CARSWELL: Yes. If he would -- either

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1 steady or expanding, he would need to acquire a base.
2 The grower who has declined -- say the grower who has
3 declined has declined from a thousand pounds of alpha
4 acid to 500 pounds of alpha acid and the cut was 50
5 percent, he would not need to acquire a base, is that
6 correct?

7 DR. FOLWELL: Correct.

8 MR. CARSWELL: Or let's even say he's gone
9 down to 10,000 pounds from a -- I'm sorry, a hundred.
10 I'm sorry, a thousand pounds to 100 pounds, then he
11 would have base allotment to sell, is that correct?

12 DR. FOLWELL: Or to rent or lease out.

13 MR. CARSWELL: I'm not sure, but I think it's
14 just the sale now, I don't think you can rest an
15 investment, but in any event, let's presume he's going
16 to sell. So he sells the 40 percent of his base that he
17 doesn't need because he was at a -- he could grow 500
18 pounds without -- alpha acid without paying -- without
19 having to buy a base, but he's only producing a hundred,
20 so he's got 400 pounds of base that he can sell and
21 grower B buys that.

22 DR. FOLWELL: How...

23 MR. CARSWELL: From an economic standpoint,
24 wouldn't this be construed as an additional cost for
25 grower -- whichever growers, the grower that has to

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1 acquire a base...

2 DR. FOLWELL: That's grower B.

3 MR. CARSWELL: Yes.

4 DR. FOLWELL: Yes, but I've observed this
5 happening under the old federal marketing order. As a
6 matter of fact, one of the largest hop growers in the
7 Yakima Valley -- I'll even name him. His name is Dave
8 Wykcoff down by Prosser, he's entered hop production
9 under the old order and he either had to rent, lease, or
10 purchase his base and he currently has a couple thousand
11 acres of hops. So it is possible for entry and to grow
12 in size.

13 ADMINISTRATIVE LAW JUDGE: Could you just
14 spell Wykcoff for me?

15 DR. FOLWELL: Oh, my. W-y-c-o-f-f.

16 MR. ROY: There's a k in it.

17 DR. FOLWELL: Is it?

18 ADMINISTRATIVE LAW JUDGE: W-y-k-o-f-f?

19 MR. ROY: W-y-c-k-o-f-f.

20 ADMINISTRATIVE LAW JUDGE: Oh, that's
21 different. W-y-c-k-o-f-f. Thank you, Mr. Roy. I think
22 we need to take a comfort break, about 10 minutes.
23 Please be back and ready to go back on record at 11:16.

24 ***

25 [Off the Record]

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1 [On the Record]

2 ***

3 ADMINISTRATIVE LAW JUDGE: We're back on
4 record now at 11:17. Mr. Carswell, one of your earlier
5 questions, identify the variety of hops grown in the
6 Czech Republic. Could you state the name of that
7 variety and spell it for us?

8 MR. CARSWELL: It's Saaz, and on the spelling
9 I'm going to have to get a little help. I think it's
10 S-a-a-z.

11 ADMINISTRATIVE LAW JUDGE: All right, anybody
12 have a contrary spelling? Saaz, S-a-a-z. Thank you,
13 Mr. Carswell. Mr. Carswell, you may resume.

14 MR. CARSWELL: Dr. Folwell, I believe we left
15 off that I had asked you whether you would describe the
16 payment for purchase of base fund grower B from grower A
17 to be an additional cost to grower B and you responded
18 with a antidotal reference to a grower who had entered
19 during the previous hop marketing order and who had had
20 to acquire a lease or rent base to do so. But if you
21 could answer my question whether you would describe that
22 as an additional by grower B, I would appreciate it.

23 DR. FOLWELL: If the base had -- oops.
24 Somebody turned me off. Is that better? If, in fact,
25 the base had value, it would add to his production cost.

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1 MR. CARSWELL: And I believe you indicated
2 that the hop marketing order would work, then indeed,
3 that base would have value, is that correct?

4 DR. FOLWELL: It could, eventually. But
5 whether it would or not initially is anybody's guess at
6 this point in time.

7 MR. CARSWELL: If it indeed had value and thus
8 resulted in higher cost for grower B, would that place
9 him at a competitive disadvantage vis-à-vis grower A?

10 DR. FOLWELL: That depends upon what grower
11 A's production costs are. They could be completely
12 different from what grower B is because he was much
13 smaller in size, there are economies of size in this
14 industry.

15 MR. CARSWELL: Presuming equal cost going in,
16 would you say that grower B would face a competitive
17 disadvantage versus grower A?

18 DR. FOLWELL: Hypothetically, yes.

19 MR. CARSWELL: If grower A used that payment
20 to reinvest in his hop growing operation, would that
21 exacerbate the competitive disadvantage that grower B
22 would be facing?

23 DR. FOLWELL: I guess my question is how would
24 you reinvest in his hop growing operation...

25 MR. CARSWELL: Yes, sir.

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1 DR. FOLWELL: ...in terms of what? New poles,
2 new wire?

3 MR. CARSWELL: Equipment. Harvesting
4 equipment. Getting state-of-the-art harvesting
5 equipment, for example.

6 DR. FOLWELL: It could.

7 MR. CARSWELL: With respect to foreign
8 competition, would grower B, with this added cost to his
9 production, be put at a competitive disadvantage versus
10 foreign growers of hops?

11 DR. FOLWELL: Possibly.

12 MR. CARSWELL: Thank you. If we could go back
13 to figure one in your paper and then if you -- and then
14 on page -- referring also to page six and seven of your
15 paper, you state at the bottom of page six that "the
16 price data from '66 through '85 when Marketing Order 991
17 was in effect, indicates that the average price of hops
18 increased or remained stable in a fairly regular pattern
19 indicating an orderly market situation." If we could --
20 and then -- well, this is -- then starting in 1986 to
21 the present, after the order was terminated -- and I'm
22 quoting your paper still. "The average price of hops
23 has increased and decreased in a roller coaster pattern.
24 Such price swings are not indicative of an orderly
25 marketing situation and often leads to a misallocation

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1 of resources." If we could then look at figure one --
2 and I'm looking at the period of the hop marketing order
3 of '77 through '85 and I don't -- either just as a
4 layman, I don't see a lot of stability there. It seems
5 like there's wild fluctuations in price.

6 DR. FOLWELL: Well, first of all, you're
7 comparing apples to oranges. Figure one is the price of
8 alpha. The -- when I referred to the prices for hops is
9 to Appendix Table A1, which is in the back on page 11.

10 MR. CARSWELL: Yes, sir.

11 DR. FOLWELL: That's what I'm referring to.
12 And if you'll notice there, basically from 1965 up
13 through 1986 the price of hops went from .45 up to \$1 --
14 well, 2.03. The order was terminated in the first part
15 of '86. After that point in time you can see how the
16 price of hops went up and down in a roller coaster
17 fashion.

18 MR. CARSWELL: And from '79 to '85 there's a
19 drastic increase in the price of hops, correct?

20 DR. FOLWELL: That was the crop failure in
21 Europe.

22 MR. CARSWELL: So that was not attributable to
23 marketing order, it was attributable to the crop
24 failure?

25 DR. FOLWELL: I believe so.

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1 MR. CARSWELL: There's a direct correlation,
2 is there not, between the price of alpha and the price
3 of hops? I mean, growers use the alpha -- I mean,
4 that's what they buy hops for, aren't [sic] they?

5 DR. FOLWELL: Correct.

6 MR. CARSWELL: So in figure one, where we see
7 between '86 and 2001, you describe this -- you've
8 described on Table A1 the roller coaster pricing, but
9 here it would seem, based on the alpha acid price, that
10 it's been a fairiy -- it's been -- the pricing changes
11 have been fairly modest between '86 and 2001, doesn't it
12 appear to be that way?

13 DR. FOLWELL: But when I talk about a roller
14 coaster fashion, I'm talking about prices going up and
15 down from year to year, where in fact, during the life
16 of the old marketing order, in fact, they either stayed
17 the same or went up every year.

18 MR. CARSWELL: Well, let's just take a
19 couple...

20 ADMINISTRATIVE LAW JUDGE: Dr. Folwell, could
21 you get just a little closer to the mike, please?

22 DR. FOLWELL: Yes, ma'am.

23 MR. CARSWELL: If you look at, for example,
24 1988 to 1989, there's a decline of somewhere less than a
25 dollar in prices, is that correct?

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1 MS. FINN: Are you referring to...

2 MR. CARSWELL: Alpha acid. Figure one. I
3 believe alpha hops are traded on an alpha acid basis, if
4 I'm not mistaken.

5 DR. FOLWELL: Correct. And what was your
6 question again?

7 ADMINISTRATIVE LAW JUDGE: I'm sorry. You're
8 talking over each other. Was your answer correct, that
9 alpha hops are traded on an alpha acid basis?

10 DR. FOLWELL: Correct. They're buying the
11 alpha acid for the...

12 MR. CARSWELL: So between '88 and '89 the
13 price was
14 -- the price change was marginal, was it not?

15 DR. FOLWELL: Yeah, there was a slight
16 decrease between '88 and '89.

17 MR. CARSWELL: And between -- it's a little
18 more substantial between '89 and '90. There's an
19 increase from between -- somewhere south of 16 to up to
20 about 17. Is that correct?

21 DR. FOLWELL: That's correct.

22 MR. CARSWELL: But between 1979 and 1980 the
23 difference was between 14 and \$22, so that was a huge
24 price swing attributable to the crop failure, correct?

25 DR. FOLWELL: Yes.

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1 MR. CARSWELL: And so the Hop Administrative
2 Committee could not, I guess, plan well enough to
3 account for the crop failure? Nobody can do that,
4 right?

5 DR. FOLWELL: Maybe you could. I couldn't.

6 MR. CARSWELL: Do you think that a free market
7 system might be able to plan a little bit better for
8 that as to compared to a centralized committee?

9 DR. FOLWELL: The assumption that this
10 industry would ever return to a competitive market
11 situation given its current structure, I think, is
12 erroneous. And furthermore, I don't think a free market
13 situation, as you would call it here, where there's no
14 interference which you called a central committee here
15 could ever project that market failure nor dampen these
16 price swings that occur. That was a result of a crop
17 failure, it was not the result of the actions of any
18 statistical committee or the Hop Administrative
19 Committee.

20 MR. CARSWELL: If you could go back to page
21 one of your report, you note, and I quote, "thus, while
22 there has been increasing concentration on the hop
23 growers on the supply side of the market, there has been
24 even further concentration in the number of dealers on
25 the demand side of the market." And that's a reference

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1 to growers going from 211 producers down to 70 and the
2 number of buyers or dealers in hops decreasing from nine
3 to four. Then you say that "these trends suggest that
4 there has been increasing market power on the demand
5 side of the market relative to the supply side with
6 producers losing market power." Hasn't there also been
7 an increase in direct purchasing by brewers such as my
8 company?

9 DR. FOLWELL: Yes. That was one of the things
10 I predicted with the termination of the last order.

11 MR. CARSWELL: Is that a good or a bad thing?

12 DR. FOLWELL: They form a vertical integration
13 in the sense that it's taking one more pricing point out
14 of the marketing channels. Some economists would say
15 it's not necessarily a good thing.

16 MR. CARSWELL: But we constitute another
17 buyer, correct?

18 DR. FOLWELL: That's correct.

19 MR. CARSWELL: So there's a -- that gets us at
20 least to five buyers at this point, correct?

21 DR. FOLWELL: Oh, correct.

22 MR. CARSWELL: And aren't there other brewers
23 who are buying direct? I believe Coors, aren't they
24 buying direct?

25 DR. FOLWELL: And some of the micro-breweries.

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1 MR. CARSWELL: Are foreign -- any foreign
2 brewers buying...

3 DR. FOLWELL: I have no knowledge of that.

4 MR. CARSWELL: Okay. So it's -- we've had a
5 consolidation of -- from 211 to 70, so we've had a -- we
6 have a third of the growers and we have at least six or
7 more buyers, so I would -- you said there's been even
8 further concentration of the number of you say dealers,
9 but if you look at it from the standpoint of buyers,
10 there's really been more concentration on the growers'
11 side than there has been on the buyers' side, isn't that
12 accurate?

13 DR. FOLWELL: That depends upon how you want
14 to measure the degree of concentration. You basically -
15 - you know, at one point in time there was [sic] 12
16 dealers, actually, in the hop market here in the United
17 States and if you looked at the market share each of
18 them had, it would be a lot smaller than what the market
19 share would be when we've only got four or five or
20 whatever you want to call in terms of buyers today.

21 MR. CARSWELL: Well, we've established there's
22 at least six buyers.

23 DR. FOLWELL: You've established, I didn't.

24 MR. CARSWELL: Well...

25 DR. FOLWELL: That's correct. I mean, if you

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1 want to separate yourself...

2 MR. CARSWELL: Separate.

3 DR. FOLWELL: Right.

4 MR. CARSWELL: Well, shouldn't we count
5 ourselves, or...

6 DR. FOLWELL: I suppose you should. I
7 wouldn't argue with that.

8 MR. CARSWELL: Okay. With respect to -- I'm
9 just going to go back to China for just one more minute,
10 okay?

11 DR. FOLWELL: Okay.

12 MR. CARSWELL: Based on your knowledge of
13 China and the hop industry, would it surprise you that
14 the vast majority of hops grown in China -- excuse me,
15 of the hops used by Chinese brewers are grown in China?

16 DR. FOLWELL: You asked that question before
17 and I said I would not be surprised.

18 MR. CARSWELL: Actually, I said a substantial
19 percentage...

20 DR. FOLWELL: Um-hum.

21 MR. CARSWELL: ...now I'm asking about a vast
22 majority. I'm sorry.

23 DR. FOLWELL: Well, I can't quantify either
24 one of those terms.

25 MR. CARSWELL: Would it surprise you that --

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1 I'm sorry. Have you ever heard of Tsing Tao Brewery?
2 The Chinese brewery?

3 DR. FOLWELL: No, I haven't.

4 ADMINISTRATIVE LAW JUDGE: Would you spell
5 that for us, please?

6 MR. CARSWELL: I believe -- I'm sorry, Your
7 Honor. I believe it's T-s-i-n-g D-a-o. But I've been
8 corrected. It's T-s-i-n-g and then the separate word T-
9 a-o.

10 ADMINISTRATIVE LAW JUDGE: Tsing Dao? Just
11 like it sounds.

12 MR. CARSWELL: Yes, Your Honor.

13 ADMINISTRATIVE LAW JUDGE: I'm joking.

14 MR. CARSWELL: Would it surprise to learn that
15 Tsing Tao is one of the largest brewers in China?

16 DR. FOLWELL: It wouldn't surprise me, but I
17 have no knowledge of it.

18 MR. CARSWELL: And would it surprise you if
19 Anheuser-Busch has a substantial interest of 20 plus
20 percent interest in Tsing Tao?

21 DR. FOLWELL: I have no knowledge of that.

22 MR. CARSWELL: And would it finally surprise
23 you if you learned that Tsing Tao exclusively uses
24 Chinese hops in its brewing operations?

25 DR. FOLWELL: It's entirely possible. I have
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1 no knowledge of it.

2 MR. CARSWELL: Thank you, Dr. Folwell. That's
3 all the questions I have.

4 ADMINISTRATIVE LAW JUDGE: Thank you, Mr.
5 Carswell. Before I go to the next questioner, I just
6 want to go back to your statement about the competitive
7 market with regard to hops. Do you consider, Dr.
8 Folwell, that the existing market is a competitive
9 market for hops?

10 DR. FOLWELL: No.

11 ADMINISTRATIVE LAW JUDGE: And why is that?

12 DR. FOLWELL: Basically because the amount of
13 market power on the producers' side, the individual
14 producers here, is a lot less than it is on the buyers'
15 side.

16 ADMINISTRATIVE LAW JUDGE: Thank you. All
17 right, the next questioner -- would that be you, Mr.
18 Moody?

19 MR. MOODY: Yes, Your Honor. Thank you.

20 ADMINISTRATIVE LAW JUDGE: All right. You're
21 welcome.

22 ***

23 CROSS EXAMINATION

24 BY MR. MOODY:

25 Q. Dr. Folwell, you described the -- you
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1 characterized the current hop industry as chaotic? Is
2 that correct?

3 A. Chaotic in the sense that it's not stable
4 in terms of the number of producers.

5 Q. Do you believe that had the marketing
6 order continued to remain in place since '85, that it
7 should have been administered in such a way as to keep
8 the number of producers relatively constant?

9 A. No, it's a fact of life in agriculture
10 that sometimes to survive you have to get larger, but in
11 this particular case there was [sic] a lot hop yards
12 that were laid idle. As a matter of fact, they're still
13 sitting out there idle, so the number of producers has
14 declined -- the lack of a market.

15 Q. All right. Is there anything that the
16 marketing order could do or even should do to keep
17 producers -- well, 211 I guess was your number -- to
18 keep 211 producers in business?

19 A. Not necessarily to keep 211 producers in
20 business, but there is the possibility of the hop
21 marketing order or the proposed order here, of creating
22 an orderly marketing situation so that the price is high
23 enough or at a level at which an average to a below
24 average size producer could remain in production.

25 Q. All right. And is it -- is that one of
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1 the intents of the order is to keep producers in
2 business, otherwise, a competitive market or go out of
3 business?

4 A. No. The intent is to create an orderly
5 marketing situation.

6 Q. All right. But -- back to my question.

7 A. I answered it.

8 Q. Okay. So it's not intended to have any
9 impact on the number of producers?

10 A. Not necessarily, no.

11 Q. How about -- is it intended to have any
12 impact on the number of dealers?

13 A. Not that I'm aware of.

14 Q. I want to -- I'm very interested in your
15 comment there were only four buyers. And I want to
16 first talk about Yakima Chief. Are you familiar with
17 that operation?

18 A. Somewhat.

19 Q. Are you aware that they -- or, take hops
20 on a consignment basis?

21 A. I don't know what the arrangements are,
22 but I do know they take hops.

23 Q. All right. And to the extent they take
24 hops on a consignment basis, then Yakima Chief would not
25 be regarded as a buyer?

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1 A. If, in fact, they're -- if it's strictly
2 a consignment and they're just doing sort of a
3 customized processing operation for a grower or
4 something, I really wouldn't consider them a buyer, in
5 that case.

6 Q. All right, then wouldn't you have to
7 count all of Yakima Chief's customers as part of the
8 buying group?

9 A. I don't quite follow your question here.
10 Your logic.

11 Q. Well, if Yakima Chief is taking hops on a
12 consignment basis, wouldn't it be correct to count all
13 of Yakima Chief's buyers as part of what you'd count as
14 the buying group?

15 A. You'd have to define for me what you mean
16 by all of their buyers. You're talking about the people
17 who consign hops to them to be sold?

18 Q. No, but that would be the growers.

19 A. That's right.

20 Q. You indicated that there were -- have
21 been an undue concentration on the buying side...

22 A. Um-hum.

23 Q. ...of the industry. I want to explore
24 that. And the number of buyers have gotten down, like
25 you said, to four major buyers. I want to test that

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1 figure. And my question is wouldn't we have to count
2 all of Yakima Chief's buyers, principally brewers, as
3 part of the buying group in examining the level of
4 concentration?

5 A. I don't believe that that's exactly the
6 way the growers would look at the marketing channels
7 they face, that would just be considered -- Yakima Chief
8 would be considered a buyer.

9 Q. Okay, but you just told me a minute ago
10 that they're -- you said if they received consignment
11 hops they would not be regarded as a buyer.

12 A. I don't know all the business
13 arrangements they have with people they receive hops
14 from.

15 ***

16 MR. MOODY: All right. Are you familiar with
17 Janicke?

18 ADMINISTRATIVE LAW JUDGE: Would you spell
19 that for us, Mr. Moody?

20 MR. MOODY: J-a-n-i-c-k-e.

21 DR. FOLWELL: I've heard of them.

22 ***

23 BY MR. MOODY:

24 Q. Do you count them as a buyer?

25 A. Yes.

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1 Q. And how about Kalsek, K-a-l-s-e-k?

2 A. I've not heard of them.

3 Q. How about John I. Haas?

4 A. I have heard of them.

5 Q. Do you count them as a buyer?

6 A. Yes.

7 ***

8 ADMINISTRATIVE LAW JUDGE: And would you spell
9 that for us, too?

10 MR. MOODY: John, like it is, I., middle
11 initial, Haas, H-a-a-s.

12 ***

13 BY MR. MOODY:

14 Q. S.S. Steiner?

15 A. Yes.

16 Q. You count them as a buyer?

17 A. Yes.

18 ***

19 MR. MOODY: Anheuser-Busch?

20 ADMINISTRATIVE LAW JUDGE: Would you spell
21 Steiner for us?

22 ***

23 BY MR. MOODY:

24 Q. S-t-e-i-n-e-r. Anheuser-Busch?

25 A. With their direct contracting, yes.

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1 Q. You count them as a buyer. And Coors, I
2 think you indicated that you count them as a buyer, as
3 well?

4 A. Correct.

5 Q. Yakima Chief -- I'm still not quite clear
6 on whether you count them as a buyer or not. They
7 receive consignment hops.

8 A. I'm not sure I would count them as a
9 buyer at this time. I'd have to know more about their
10 business arrangements with who they're receiving hops
11 from.

12 Q. LupeX? L-u-p-e-x.

13 A. I'm trying to remember -- I'm not sure
14 about them.

15 MR. BARTON: Can we go off record a moment?

16 ADMINISTRATIVE LAW JUDGE: Yes. Do you need
17 to change the tape?

18 ***

19 [Off the Record]

20 [On the Record]

21 ***

22 ADMINISTRATIVE LAW JUDGE: All right, we're
23 back on at 11:39. Mr. Moody?

24 ***

25 BY MR. MOODY:

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1 Q. Okay, we were talking about Lupex, Dr.
2 Folwell.

3 A. I have no knowledge of them.

4 Q. Lupofresh? L-u-p-o-f-r-e-s-h.

5 A. I believe they purchased hops in the
6 past.

7 Q. Do you count them as a buyer?

8 A. If they're still in the business.

9 Q. Hesselberger? H-e-s-s-e-l-b-e-r-g-e-r.

10 A. I have no knowledge of them.

11 Q. Sierra Nevada?

12 A. I have no knowledge of them.

13 Q. Anchor Brewing Company?

14 A. I have no idea how they acquire their
15 hops or extractor pellets.

16 Q. Hop Union [ph]?

17 A. I don't what their business arrangements
18 are right now, to be honest with you.

19 Q. How would you count the 900 or so micro-
20 breweries that previous witnesses testified to? Would
21 you count them as buyers?

22 A. They're eventual end-users of hops. How
23 they actually acquire their hops, I'm not sure.

24 Q. If they acquire them directly from
25 producers or on a consignment basis from something like

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1 Yakima Chief or Hop Union, would you count them as
2 buyers?

3 A. Possibly.

4 Q. All right. A couple of questions about
5 China. I may be pronouncing this wrong, but Xin Jing,
6 X-i-n J-i-n-g, are you familiar with that region in
7 China?

8 A. No, I'm not.

9 Q. Or the Western China Hop Company?

10 A. I -- no. I only am aware of the fact
11 that quite a few of the hops are produced in western
12 China.

13 Q. Are you aware of the fact that they
14 recently installed a state-of-the-art palletizing
15 operation?

16 A. No, I'm not.

17 Q. Are you aware of the fact that they
18 recently starting planting the high alpha varieties of
19 hops, the TCT [ph] varieties?

20 A. No, I'm not.

21 Q. And that they -- are you aware of the
22 variety of hops known as Marco Polo?

23 A. No.

24 Q. Are you aware of the fact that there's
25 been in -- recently, in the last two or three years,

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1 some expansion -- some brewers have expanded their
2 operations as well as new brewers have entered the
3 industry?

4 A. I'm aware of the -- some expansion, I
5 believe, in northern Idaho by a brewer.

6 Q. All right. And some expansion in
7 Washington State, as well?

8 A. I don't have any great knowledge of that.

9 Q. Well, wouldn't that be a sign of health,
10 economic health of an industry if there is expansion
11 going on and new investment?

12 A. From a -- with the brewer making the
13 investment, I consider that backwards integration.

14 Q. All right, but what...

15 A. And replacing what I would call consider
16 traditional hop producing.

17 Q. All right, what about buying...

18 A. Excuse me? I don't understand your
19 question.

20 Q. Brewers are expanding that are not owned
21 by brewers. Would you consider a sign of health in the
22 industry?

23 A. Possibly. If that's the best use of
24 their resources.

25 Q. You indicated you believe prices have

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1 been more variable since termination of the marketing
2 order? Is that correct?

3 A. I believe that they've been more on a
4 roller coaster pattern than they were before, when we
5 had the marketing order.

6 Q. Isn't some degree of price variability
7 useful in terms of sending expansion and contracts
8 singles to an industry?

9 A. Except when they become extremely
10 significant and then the problem that occurs here is
11 that when growers are attempting to obtain financing for
12 their operations, sometimes bankers are not willing to
13 loan the money to these growers.

14 Q. Do you have an opinion of what level of
15 variability in this industry constitutes an unreasonable
16 fluctuation in supply or price?

17 A. Not here today, I don't.

18 Q. Have you done a variability analysis pre
19 and post termination of the old order?

20 A. No, it's just been observation of the
21 price trends that occurred as is shown in Appendix Table
22 1.

23 Q. All right. I notice in your appendix,
24 those appear to be nominal dollars, not constant
25 dollars?

1 A. That's correct.

2 Q. Any particular reason you didn't convert
3 those to constant dollars?

4 A. If I had converted them to constant
5 dollars, there would be some variation up and down in
6 terms of those prices, but given the fact that producers
7 respond to nominal prices when they're making production
8 decisions and not real prices or deflated prices, I
9 didn't.

10 Q. You indicated that the overall industry
11 had been overoptimistic in making its demand projection
12 and overly pessimistic in making its supply projection,
13 is that correct?

14 A. I would say that they had a philosophy of
15 always trying to increase their market share worldwide
16 in terms of trying to say that they thought the sales or
17 the consumption would be there, yes.

18 Q. And what -- given your observation, what
19 effect did your observation have on the committee
20 setting of the saleable?

21 A. Basically, I thought they often set the
22 saleable a little bit higher than they could've. In the
23 situation existing under the old order, there was a
24 dealers advisory committee to the Hop Administrative
25 Committee. They were non-voting members. They sat at a

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1 different table, just like we are here, and they would
2 often make projections where they trying to increase the
3 availability of hops much more than what the HAC did. I
4 thought that the brewers -- or the brewers -- the
5 dealers' projection were way too high in terms of the
6 availability of hops, which they wanted, where the HAC's
7 was more in line to create an orderly marketing process.

8 Q. So in you view, should the saleable have
9 been set lower under the old order?

10 A. No, not necessarily, because they had a
11 basic philosophy throughout, if you go back and read the
12 minutes of the meeting, that they constantly wanted to
13 increase their market share around the world and you
14 can't increase your market share unless you've got a
15 product to sell.

16 Q. I'm trying to understand the connection
17 between your observation and the saleable. I mean, it
18 -- you think the saleable was set correctly under the
19 old order?

20 A. Given their philosophy of trying to
21 increase their market share, yes.

22 Q. From an agricultural economist's point of
23 view, is that the correct...

24 A. I don't think it was unacceptable at
25 which they were attempting -- what they were attempting

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1 to do in terms of trying to increase the sales
2 worldwide.

3 Q. Now you also, I think, mentioned the term
4 greed, that the committee got greedy at some point in
5 time?

6 A. Not the committee. I think everybody in
7 the hop industry had a certain amount of greed surface
8 in their behavior.

9 Q. Okay, and what effect did that have on
10 setting the saleable?

11 A. For the official saleable, it was
12 published in the Federal Register, but what happened was
13 that a few hop growers -- actually, a few, I should say.
14 I can't give you an exact number, but at least one hop
15 grower I know of went out and sold his entire base and
16 then came back to the administrative committee and says
17 give me more base for nothing. And the answer was no.

18 Q. All right. Did this greed amongst
19 members of the industry cause the saleable to be set too
20 high?

21 A. Not for what was published in the Federal
22 Register. I think there was an expectation on the part
23 of the growers beyond when the saleable percentage was
24 published in the Federal Register that it would not be
25 cut back on and a lot of growers went out and signed

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1 multiple-year fixed-price contracts, which were at the
2 saleable set for the particular marketing year. I
3 believe it got up to 130 percent and growers were
4 basically going out and signing contracts at 130 percent
5 saleable when, in fact, if one would sit back and look
6 at the projections of supply and demand beyond one year
7 and realizing that the Hallertau region and other areas
8 in Europe were going to come back into production, that
9 that market demand was not going to be there.

10 Q. Could you describe this Sun River
11 agreement?

12 A. I didn't know there was an agreement. I
13 was there at Sun River in October of '79.

14 Q. Okay. And what's your understanding of
15 what occurred there?

16 A. At that particular administrative
17 committee meeting in October of '79, the saleable
18 percentage was recommended to the Secretary of
19 Agriculture through his representative to the committee
20 that it be set at 130 percent. There was discussion
21 about the fact that they hoped that the market would
22 continue at that level in future beyond what they were
23 setting the saleable for that particular marketing year.

24 Q. And wasn't there a general understanding
25 that the saleable would be kept at that level for the

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1 next few years?

2 A. I don't -- well, there was talk of it,
3 let's put it that way, but there could be nothing
4 officially on those lines.

5 Q. And a lot of brewers expanded their
6 production in response to the higher saleable?

7 A. They did, because of the prices and the
8 contracts that dealers were offering.

9 Q. All right...

10 A. And that's when the acreage went up to 50
11 some thousand acres here in the US and then realizing
12 that the market demand was not there there's, you know,
13 20 some thousand acres have been idle, and that's a big
14 misallocation of resources as I indicated earlier.

15 Q. Now did that result in an oversupply and
16 an increase in the carry-in percentages?

17 A. In terms of the stocks, yes. Stock
18 levels started increasing.

19 Q. And do you have a view as to what the
20 desired level of carry-in is?

21 A. That has changed over time. When we're
22 not in this world of alpha and we're talking about aroma
23 hops, et cetera, basically the desirable level of stocks
24 was approximately two years. The brewers wanted to make
25 sure that they had an adequate supply of hops, even if

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1 there was a crop failure. So there was sort of a target
2 there of having at least two years on hand in case some
3 disease, pest, or something else would invade the
4 industry. With the introduction of the high alpha
5 varieties, and I should say simultaneously, all of this
6 happened at the same time, the concern about the
7 production of alpha instead of the production of pounds
8 of hops, that was all changing at the same time, from
9 the late '70s into the early '80s, and all at once now
10 we had products with new technology where the hops were
11 storable for more than just a year and still had
12 adequate characteristics for brewing. So there was a
13 change in philosophy about the level of stocks we
14 actually needed. And the stock level went -- because of
15 the alpha varieties and because of the processing, the
16 palletizing the extract, went much higher than was
17 probably needed by the industry.

18 Q. It occurred during the mid-'80s?

19 A. Correct.

20 Q. Carry-in got too high?

21 A. Correct.

22 Q. Okay. Well, what was -- at that time,
23 what was the desirable level of carry-in? Two years?

24 A. No. I think it was something less than
25 that. It was probably down closer to one year.

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1 Q. Okay. Now, has that changed since then?

2 A. Probably not much. I mean, in terms of
3 the one year. That's probably a reasonable level of
4 stocks.

5 Q. And you indicated that the spot market
6 price jumped quickly from .75 cents a pound to \$6 a
7 pound?

8 A. Yes, it did.

9 Q. And what percentage of the hops were sold
10 on the spot market?

11 A. A very small percentage. There weren't
12 that many really available out there, but this was the
13 price signal that the producers were receiving and
14 that's what they responded to.

15 Q. All right. Like under five percent?

16 A. I would probably say less than 10
17 percent. I don't know if it was five percent. It was
18 probably less than 10 percent.

19 Q. All right. So that spike in the spot
20 price didn't affect the contract price, though?

21 A. The contract prices went up after the Sun
22 River meeting.

23 Q. And...

24 A. The multiple-year contracts and the
25 prices offered with those multiple-year contracts went

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1 up.

2 Q. Now, is that a result of the crop
3 failure, or is it a result of the agreements at Sun
4 River?

5 A. I think it was more a function of the
6 crop failure and the fact that, in particular, I don't
7 know why, but why the industry felt that Europe would
8 not come back was false because if hop production was
9 the highest and best use of those resources in Europe,
10 even though they had a crop failure, those producers
11 were going to come back into hop production. They
12 weren't going to switch over to wine grapes or
13 something.

14 Q. All right. Now, hasn't the technology
15 changed since the end of the old order to make hops much
16 more storable in terms of being stored as alpha acid
17 than in terms of just leaf hops?

18 A. Yes, sir.

19 Q. And how has that affected the market?

20 A. Well for one thing, they're now pricing
21 at an alpha instead of just, you know, pounds per --
22 pounds of hops in general. It's also reduced the need
23 for having two years of carry-in or stocks or hand.
24 There's been, you know, multiple changes there.

25 Q. But doesn't -- isn't the storability of a
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1 commodity like hops a market mechanism to provide
2 stability and reduce risk?

3 A. Would you say that again?

4 Q. Isn't the storability of a commodity like
5 hops a free market mechanism that can reduce instability
6 and risk?

7 A. It can. There is [sic] many demands for
8 stocks, both by brewers as well as people speculating in
9 the market, et cetera, so there's lots of reasons and
10 different demands for holding stocks.

11 ***

12 MR. MOODY: All right...

13 ADMINISTRATIVE LAW JUDGE: Mr. Moody, just so
14 the typist gets this right, you've been using the term
15 carry-in?

16 MR. MOODY: Yes.

17 ADMINISTRATIVE LAW JUDGE: And you would spell
18 that c-a-r-r-y - i-n?

19 MR. MOODY: Yes.

20 ADMINISTRATIVE LAW JUDGE: All right. And
21 that's what you said, also, Doctor?

22 DR. FOLWELL: Um-hum.

23 ADMINISTRATIVE LAW JUDGE: Thank you. Go
24 ahead.

25 ***

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1 BY MR. MOODY:

2 Q. All right. So the ability of the
3 industry since the termination of the old order to store
4 hops at -- in the form of alpha acid is a stabilizing
5 feature of the free market?

6 A. It's a stabilizing feature of the
7 industry, that's correct.

8 Q. All right. And what waste of hops has
9 been occurring since termination of the old order?

10 A. Waste?

11 Q. Yes.

12 A. I'm not sure what you mean by waste.

13 Q. Well, sometimes when people speak of
14 mechanic marketing conditions, they end up talking about
15 waste of a commodity, it's thrown out or disposed of or
16 used as salvage.

17 A. Um-hum. What amount of -- I think
18 there's been a trend towards only harvesting those hops
19 which are -- have enough alpha in order to justify the
20 processing the costs. If you want to consider
21 un-harvested acreage as waster, that would be one
22 example.

23 Q. But isn't that a rational decision to
24 make by the farmer who didn't necessarily have a
25 contract for those hops?

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1 A. Not necessarily didn't have a contract,
2 but at the time of harvest, the hops didn't have the
3 characteristics that would justify the process.

4 Q. Do you have examples of that happening
5 recently?

6 A. Yeah, I can take you out here on the
7 highway at Bean Road [ph] and show you a hop yard that
8 wasn't harvested this year.

9 Q. Okay. And is -- but it was the producer
10 who made that decision. Made it on the basis of
11 deciding to save some money.

12 A. Of not incurring the cost of processing
13 and because of the low alpha.

14 Q. That's correct. Presumably he didn't
15 have a contract?

16 A. I don't know if the individual had a
17 contract or not for those hops.

18 Q. All right. Could it also have been a
19 baby production year?

20 A. The -- you're referring to baby hops,
21 when in fact, we used to get a partial crop in the first
22 year, I'm not sure of that.

23 Q. In preparing your testimony, did you work
24 out any scenario as to how the saleable would be set had
25 the order been placed, say, starting in 2000 to examine

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1 the economic effects of how the order would operate?

2 A. No, sir.

3 Q. Had it been in operation since 2000,
4 would the inventories, carry-in inventories, had been
5 lower, in your view?

6 A. Possibly. It would depend upon what
7 arrangements were made for producers to put the hops
8 into a reserve or whatever. It's a hypothetical
9 question, because I don't know how the order would've
10 operated from 2000 forward.

11 Q. Well, to the extent the carry-ins
12 would've been lower, isn't it true that the industry
13 would've given up its profit opportunity because of the
14 current crop failure in Germany?

15 A. That's possible, but there's a cost
16 associated with carry-in inventories to take advantage
17 of those opportunities and most people who have a demand
18 -- a speculative demand for carry-ins or stocks, I would
19 say in most industries are a definite minority and there
20 wouldn't be a great opportunity for the industry,
21 overall, to enjoy that opportunity.

22 Q. Do you have a projection of what the
23 proper value of base should be?

24 A. No, I don't.

25 Q. Do you recall, under the old order, what
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1 -- how expensive base got?

2 A. The highest price I ever heard of -- and
3 of course, these were never recorded or anything else,
4 this was probably over a bottle of beer after an HAC
5 meeting -- was that I heard prices of \$2 a pound.

6 Q. All right. And then express those on an
7 alpha acid basis for a high-yielding variety, say 15
8 percent. Wouldn't that be \$30 a pound?

9 A. It could be.

10 Q. All right, and -- so the price of base,
11 to set it that high, would be equal to the entire cost
12 of sale of that pound of alpha acid in a given year.

13 A. It could be, yes.

14 Q. All right. And to the extent a grower
15 had to acquire a base in order to sell his hops,
16 wouldn't that tend to discourage innovation?

17 A. It could, but at the same time we had
18 entry of new growers and we also had existing growers
19 who were going out and buying base and selling hops.

20 Q. Since the old order was terminated,
21 haven't there been a variety of technological
22 innovations in the industry?

23 A. Yes.

24 Q. Including the development of higher alpha
25 acid varieties?

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1 A. Correct.

2 Q. And the installation of new extracting
3 plants?

4 A. Correct.

5 Q. And improved palletizing equipment?

6 A. Correct.

7 Q. And all these occurred under the free
8 market?

9 A. All these occurred under the industry
10 that exists right now. I don't know if you want to call
11 it a free market.

12 Q. All right. Hasn't the -- by reducing
13 acreage, hasn't the industry largely adjusted to the
14 drop in brewer demand for hops?

15 A. I would say yes. There's been a major
16 adjustment in this industry, with fewer growers and
17 fewer acres.

18 Q. And one of the opponent's witnesses
19 testified last week that in his view, the industry was,
20 at least at the moment, in '03, in balance? Would you
21 agree with that?

22 A. No.

23 Q. And why's that?

24 A. Because basically the price of hops is so
25 low right now that I would say there's an oversupply

1 situation.

2 Q. And how is that oversupply expressed? It
3 is expressed in carry-ins that are too high?

4 A. Carry-ins are too high and prices are too
5 low.

6 Q. Well, what is the current price for hops?

7 A. Today?

8 Q. Yes.

9 A. I don't know. I know of hops during this
10 past year, some of them were selling down between .25
11 and .50 cents a pound.

12 Q. And given the crop failure in Germany,
13 has the price gone up?

14 A. It could. I don't follow the hop market
15 daily.

16 ***

17 MR. MOODY: I think that's all for now.

18 Thanks, Dr. Folwell.

19 DR. FOLWELL: Thank you.

20 ADMINISTRATIVE LAW JUDGE: Other questions for
21 those -- from those who are here in a position against
22 the proposals? Mr. Carswell?

23 MR. CARSWELL: Just a couple of quick
24 questions. You mentioned between the two of you, that
25 on an alpha basis, if the base was \$2 a pound for 15

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1 percent alpha, that it could be -- the purchase of base,
2 it could be \$30 a pound for the acquisition of base?

3 DR. FOLWELL: I assume Mr. Moody was taking
4 two times 15.

5 MR. CARSWELL: Wouldn't that result in a very
6 large competitive disadvantage with respect to a near
7 perfect substitute coming in from -- or not coming in,
8 but competing with a near perfect substitute from, say,
9 Germany?

10 DR. FOLWELL: It would appear to on the
11 surface, but yet I observed growers during the last
12 marketing order go out and pay the equivalent for base
13 of what the hops were selling for in dollars per pound.

14 MR. CARSWELL: When were they doing that?
15 What years are we talking about?

16 DR. FOLWELL: Oh, I would say probably '80,
17 '81, '82, sometime in there.

18 MR. CARSWELL: So wasn't that in response to
19 the German crop failure? Is that what made that
20 profitable?

21 DR. FOLWELL: It was in response to the spike
22 in the price that occurred in what the dealers were
23 offering to the growers.

24 MR. CARSWELL: Thank you, sir.

25 ADMINISTRATIVE LAW JUDGE: Dr. Folwell, is the
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1 global market today considerably different from what it
2 was 20 years ago?

3 DR. FOLWELL: I would -- yeah, I would say so.
4 There's a -- for instance, the entry of China into hop
5 production and actually exporting what I referred to as
6 food-grade vegetative matter to the industry here. The
7 European economy has changed. The politics over there
8 have changed. The setting of agricultural policy has
9 changed, so yes, you know, things have changed. The
10 world has not stood still.

11 ADMINISTRATIVE LAW JUDGE: There's been
12 mention that we might take official notice of the
13 contents of the hearing that led to the termination of
14 the old order. Do you believe there are so many
15 variables between then and now that it would be
16 difficult for that information to be useful or do you
17 think there is use for it?

18 DR. FOLWELL: Well, I'm not quite sure what
19 information you're referring to at the time. I think
20 that one of things that occurred that was not
21 necessarily a good thing was that the industry was
22 supposed to be working in partnerships with the USDA and
23 the Secretary of Agriculture and that became an
24 adversary-type relationship. The industry was sort of
25 -- I don't know how to exactly say this, but they were

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1 sort of frustrated, sort of stressed out over the
2 position that the federal government was taking about
3 federal marketing orders with producer allotments.
4 There was a lot of press releases that started an anti-
5 marketing move at that time. For instance, in Time
6 magazine there was an article which had a huge pile of
7 oranges in California and they were saying it was
8 because of these marketing orders that those oranges
9 were not being sent to the needy kids in New York City.
10 Well, the truth of the matter was those oranges were
11 hardly suitable for even processing, let alone shipping
12 to a fresh market. There was just, at that point in
13 time, seemed to be a lot of anti-marketing type behavior
14 going on in the US and it created a level of frustration
15 which was interesting to observe.

16 ADMINISTRATIVE LAW JUDGE: And so there was a
17 lot of sentiment against efforts to influence supply?

18 DR. FOLWELL: I believe there was, yes.

19 ADMINISTRATIVE LAW JUDGE: And do you have any
20 statistical information for how much supply -- what
21 percentage of supply needs to be available to be
22 influenced for it to have an impact in the market?

23 DR. FOLWELL: In terms of depressing the
24 market prices, I think that any time that you have a
25 production level in a given year and the carry-in stocks

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1 that are not sufficient to meet the demands in the
2 market, both domestically and internationally, that it's
3 going to have an impact on price. There's just no doubt
4 about it. If that overall supply in terms of from
5 domestic production, from stocks as well as imports,
6 fall short of what the demand is, there's going to be an
7 increase in price and vice versa. If the demand
8 components, in terms of the domestic demand for hops,
9 the export demand for hops, the demand for hops in
10 storage exceeds the supply, you're going to see a major
11 increase in price.

12 ADMINISTRATIVE LAW JUDGE: If the US controls
13 -- or rather, excuse me, if the US supplies 50 percent
14 of the world supply of hops, the influence, then, on
15 price could be substantial.

16 DR. FOLWELL: If, in fact, our market share
17 was that high, but it's really not. We talked earlier -
18 - there was about -- in 2003 at least, as of, I don't
19 know, August 5, they were talking about 54 million
20 pounds from the US and worldwide it was 239 million
21 pounds. So we're not 50 percent of the world hop
22 industry.

23 ADMINISTRATIVE LAW JUDGE: Have you given any
24 thought to what impact on the marketing order proposal
25 it would cause if aroma hops were exempted from its

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1 provisions?

2 DR. FOLWELL: No, not -- I really haven't. I
3 mean, the concern has, you know, has been stated to me
4 in other places has been the alpha hops, the varieties
5 high in alpha. But I think that the -- you know, part
6 of this picture is also the aroma hops. As one dealer
7 said to me one time in Portland during a meeting, he
8 says you know, he says, you can't even tell what variety
9 of hops went into a beer -- into most beers because most
10 of them are pasteurized. So yes, a hop -- unless, you
11 know, if you have un-pasteurized beer, is different.
12 But a hop tends to be a hop in terms of its alpha acids
13 and it's ability to flavor malted beverages.

14 ADMINISTRATIVE LAW JUDGE: And so the
15 distinctiveness of an aroma hop is lost in
16 pasteurization?

17 DR. FOLWELL: In terms of the variety it is.
18 In terms of the taste of the beer, in terms of the
19 hopping ratio that the particular brewer, brew master,
20 uses, I think most experts in the beer industry can tell
21 you approximately, you know, how many pounds of hops
22 were used per barrel of beer, et cetera. But in terms
23 of the actual variety, not necessarily.

24 ADMINISTRATIVE LAW JUDGE: And is there any
25 use of hops other than in brewing beer that you're aware

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1 of?

2 DR. FOLWELL: A little bit of pharmaceutical
3 use and I have one. It's a good weed killer at times,
4 too. I've watched a hop vine kill weeds if you lay it
5 down next to them.

6 ADMINISTRATIVE LAW JUDGE: Thank you.
7 Additional questions from those who are here in a
8 position against the market order proposals? There
9 being none, I'd now like to turn to those who are in a
10 neutral position, beginning with representatives of
11 USDA. Dr. Hinman?

12 DR. HINMAN: Good afternoon, Dr. Folwell.

13 DR. FOLWELL: Hello, Don.

14 DR. HINMAN: Well, the first two questions
15 actually relate to sort of a clarification of terms you
16 used. And one was -- this is a new one to me --
17 grubbing. Would you spell that and explain that?
18 What...

19 DR. FOLWELL: G-r-u-b-b-i-n-g. It's a policy
20 within the European community to actually pay producers
21 for removing hops.

22 DR. HINMAN: Okay.

23 DR. FOLWELL: To plow them out.

24 DR. HINMAN: And what years was -- is that
25 common in the past?

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1 DR. FOLWELL: Yeah, it was very common. I'd
2 often hear about it during HAC meetings from the late
3 '70s into the mid-'80s.

4 DR. HINMAN: Okay. You mentioned the
5 balancing item as an issue that was, I guess,
6 problematic or represented a problem in accounting.
7 Could you discuss that?

8 DR. FOLWELL: There really wasn't a problem.
9 Basically, what it was is that once they put together
10 all of the -- their projections of the components of
11 supply and demand, and since they were basically working
12 -- using a formula, or a balance sheet, which I'm sure
13 you have seen, where they've got all the demand
14 components and all the supply components, when they
15 would project those out, they wouldn't come -- they
16 wouldn't equal each other exactly. So we used to -- I
17 used to joke with them and say well, it's plus two
18 million this year and next year it'll be a minus two
19 million. It's just because their projections did the
20 aggregate of their projections on the demand side didn't
21 equal the aggregate of their supply projections. And it
22 was just an item put in there to make sure supply equals
23 demand. And it was usually a very minor quantity that
24 was put in there.

25 DR. HINMAN: Thank you. I want to ask some

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1 particular, basically, some source and clarification
2 numbers from your paper.

3 DR. FOLWELL: Sure.

4 DR. HINMAN: On page one near the top, you
5 mentioned the cost figures. If you could state what the
6 source of those cost figures were.

7 DR. FOLWELL: If you look at page nine of my
8 report, there's a complete reference to everybody I
9 cite. Herb Hinman, who is a colleague of mine, a
10 faculty member at Washington State University has been
11 doing these hop marketing studies for establishment
12 production for, I don't know, 15, 20 years it seems
13 like. And he basically meets with producers and
14 establishes a common cultural practice, collects the
15 input prices and puts together these cost of production
16 budgets.

17 DR. HINMAN: I think I may have to go explore
18 whether he may be a long lost relative.

19 DR. FOLWELL: Oh, okay.

20 DR. HINMAN: Do you have that study available?

21 DR. FOLWELL: In my office, yes. Or I can
22 make them available.

23 DR. HINMAN: In the middle of the page there,
24 you talk about the decline in the number of producers to
25 about 70. Could you state the source of that number?

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1 DR. FOLWELL: Basically, in talking to hop
2 producers, I believe, who actually, I think, conducted a
3 survey of sort of a pull straw vote on this proposed
4 marketing order this past summer. I understand now it's
5 less than that, though, now.

6 DR. HINMAN: Do you have a more recent
7 estimate?

8 DR. FOLWELL: I don't have one, no.

9 DR. HINMAN: On the bottom of page two, you're
10 referring to the thesis by Habuki...

11 DR. FOLWELL: Um-hum.

12 DR. HINMAN: And you mention the spot market
13 price elasticity of what, minus -- with respect to total
14 US hop production of -3.3. My question relates to
15 understanding which price you're talking about. You
16 said spot market price and I'm trying to relate that to
17 then, the season average grower price in nominal terms
18 that you have in your appendix. Is that the same,
19 different? Can you explain that difference?

20 DR. FOLWELL: It's different. In the
21 econometric model, we actually had a price equation for
22 those hops sold on the spot market. That information or
23 statistics, it was readily available from the Hop Market
24 News published by the USDA, where we would obtain that,
25 and of course, then the direct price elasticities that

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1 we're talking about are on those that were sold under
2 contract.

3 DR. HINMAN: Thank you. On page six, towards
4 the bottom, you talk about -- you're quoting your own
5 paper there -- "price variability during the life of the
6 present order has been less than half that experienced
7 otherwise." I just want to ask was that computation
8 made or, you know, your estimate related to just
9 comparing the period with the order to without the
10 order, or was there any kind of estimation made of the
11 factual. A model to say what it would have been without
12 the order.

13 DR. FOLWELL: No, it was not -- we made no
14 computations as to what it would've been without the
15 order. It was the price variability within the life of
16 the order versus what had existed previous to that. You
17 have to realize that was done in the early 1980s.

18 DR. HINMAN: On page seven you mention the
19 impact of the federal order on the price of beer and I
20 believe you're -- I want to make sure you're referring
21 to, I believe the same estimate that appears on page 13
22 and you actually gave that number for...

23 DR. FOLWELL: Right.

24 DR. HINMAN: ...12-ounce model? Can you
25 explain that computation?

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1 DR. FOLWELL: What that was based upon was, at
2 the particular time when I wrote that, it was what the
3 base was trading for under the old marketing order, then
4 taking into account what the hopping rate was in terms
5 of the pounds of hops that went into a 31-gallon barrel
6 of beer and then just carrying it forward to how many
7 12-ounce bottles or cans of beer you're going to get
8 from that 31-gallon barrel.

9 DR. HINMAN: Okay, so...

10 DR. FOLWELL: A very simplistic way of looking
11 at it.

12 DR. HINMAN: It was an estimate of the value
13 of base at the time.

14 DR. FOLWELL: Um-hum.

15 DR. HINMAN: And do you remember that number?

16 DR. FOLWELL: At this time, I would guess some
17 place between a dollar and a quarter and \$2. And I gave
18 that number to the USDA at a hearing right up the street
19 here in the Cascade Natural Gas building back in the
20 early 1980s.

21 DR. HINMAN: I want to then go to the
22 elasticity estimates...

23 DR. FOLWELL: Um-hum.

24 DR. HINMAN: ...that have been discussed.

25 Could you state, you know -- basically what I'm getting

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1 at is your view based on your price elasticity estimate
2 of the actual -- what's the meaning of that figure in
3 terms of what -- either a specific number or just a
4 general observation about what that figure means in
5 terms of total revenue to growers within/without a
6 proposed order?

7 DR. FOLWELL: Well, basically, if we assume
8 based upon this and Habuki's study that the demand is
9 inelastic with respect to price, that any decrease
10 actually in the quantity of hops flowing to the market
11 will result in an increase in total revenue to the
12 industry.

13 DR. HINMAN: Thank you. On the top of page
14 six of your paper you had previously referred to
15 Habuki's evidence of the demand for elasticity and the
16 demand for hops and then you refer here to the demand
17 for US hops. Is it specifically, in this case, the
18 demand for alpha acid? In this case?

19 DR. FOLWELL: In my particular case?

20 DR. HINMAN: Yeah, in the...

21 DR. FOLWELL: In my case that equation does
22 have alpha acid. It's not based upon...

23 DR. HINMAN: But in a sense, it could be a
24 demand for alpha acid is inelastic and do you think, in
25 this case, does it make any difference here? Is your

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1 basic conclusion the same?

2 DR. FOLWELL: It's the same.

3 DR. HINMAN: But this particular case is alpha
4 acid...

5 DR. FOLWELL: Correct.

6 DR. HINMAN: You had made a statement and I'm
7 not finding the exact page, about with a more reliable
8 supply and less risk, the cost of marketing is less
9 aiding in overall efficiency.

10 DR. FOLWELL: That must come from another --
11 not this report. I don't believe...

12 DR. HINMAN: Okay. I guess I thought I'd seen
13 it in that paper. Referring to the model itself. In
14 developing this model of the demand for alpha, did you
15 consider including some other variables typically
16 involved in demand estimations such as income?

17 DR. FOLWELL: I actually have the printouts
18 with me. I have to go back through them, but I did try
19 other things such as the production of beer, which was
20 in the Sparks report. I can't remember whether I
21 actually tried income in there or not. I probably did,
22 because it's a readily available statistic.

23 DR. HINMAN: But whatever it is you did, it
24 did not yield adequate results?

25 DR. FOLWELL: It didn't -- it probably was not

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1 significant and/or wrong sign according to economic
2 theory.

3 DR. HINMAN: Okay. In the three, you know,
4 talking variables, the binary variables you used there,
5 there is a substantial difference in terms of the
6 statistical significance at a given level of probability
7 of one and two versus three. Could you comment on that
8 and what level of probability would apply to the
9 statistical significance of D3?

10 DR. FOLWELL: Well, there's no doubt that, in
11 terms of the probability level that it would be
12 associated with, it would be a lot less with D3 than it
13 would be with the other ones. However, in terms of
14 hypothesis testing, one has to set a significance level
15 to be a true scientist, before you actually do the
16 hypothesis testing and it's been my experience with
17 econometric models that at any time that you have a t-
18 value that's greater than 1 in absolute value in here,
19 that if you have economic justification for keeping it
20 in the model, to go ahead and do it. However, coming
21 back to your original question. To say which of these
22 variables is more significant than the other, a
23 statistician will tell you you cannot, given the t-
24 values. They're either significant, or they're not
25 significant.

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1 DR. HINMAN: Okay. Thank you.

2 MR. BARTON: Can we go off record a moment and
3 change?

4 ADMINISTRATIVE LAW JUDGE: Yes, let's go off
5 record at 12:22.

6 ***

7 [Off the Record]

8 [On the Record]

9 ***

10 ADMINISTRATIVE LAW JUDGE: We're back on the
11 record at 1:30 p.m. We were last talking on record at
12 12:22. We took our lunch break and also, Mr. Monahan,
13 would you indicate what you have distributed?

14 MR. MONAHAN: Yes, Your Honor, I've...

15 ADMINISTRATIVE LAW JUDGE: Can't hear you.

16 MR. MONAHAN: Can you hear me now? No? Can
17 you hear me now?

18 ADMINISTRATIVE LAW JUDGE: No. It's not on at
19 all.

20 MR. MONAHAN: That doesn't sound promising,
21 does it?

22 UNKNOWN: Is that on there? Is this one on?

23 MR. MONAHAN: Well -- oop, there we go.

24 ADMINISTRATIVE LAW JUDGE: There. Excellent.

25 MR. MONAHAN: How's that? Can you hear me

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1 now?

2 ADMINISTRATIVE LAW JUDGE: Yes.

3 MR. MONAHAN: All right. Your Honor, we were
4 make copies of Identifications 27, 28, and 29, which
5 were identified for the record earlier by Dr. Folwell.
6 I have handed copies of the original to the court
7 reporter for the purposes of allowing the witness to
8 retain the originals. I have also delivered copies of
9 those three identifications to representatives for the
10 USDA, counsel for the opposition, as well as the
11 professional witnesses in attendance.

12 ADMINISTRATIVE LAW JUDGE: All right. I need
13 for someone, preferably, Dr. Folwell, although it's a
14 little beneath him to do it, to compare the original
15 with the copy that has become the official copy to make
16 sure they are duplicates. I know that'll take a little
17 time, but that will give the participants here who have
18 copies of those exhibits a chance to look at them. So
19 let's go off record while that comparison is made. And
20 we can decide whether we really need to take his only
21 original from him. I'm not sure we have to do that.

22 ***

23 [Off the Record]

24 [On the Record]

25 ***

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1 ADMINISTRATIVE LAW JUDGE: Okay. Are we back
2 on record? All right, we're back on record at 1:35.
3 Dr. Folwell, in which exhibit did you find some of the
4 footnotes not to have copied completely?

5 DR. FOLWELL: 28.

6 ADMINISTRATIVE LAW JUDGE: Exhibit 28. Can
7 you tell us on what pages the copy is incomplete and
8 what also shows on the original that does not show on
9 that copy?

10 DR. FOLWELL: On page 11 the last line of the
11 footnote did not copy very well.

12 ADMINISTRATIVE LAW JUDGE: What does it read
13 on the original?

14 DR. FOLWELL: It says -- the whole line says,
15 "for the government to reduce the value of land used in
16 producing other."

17 ADMINISTRATIVE LAW JUDGE: Thank you. On that
18 exhibit, was that the only discrepancy you found?

19 DR. FOLWELL: Yes.

20 ADMINISTRATIVE LAW JUDGE: Okay, I'd like to
21 know from those participants whether we can take it as
22 the official record copy, the one that's slightly
23 incomplete in that respect so that Dr. Folwell may keep
24 his original. Mr. Carswell?

25 MR. CARSWELL: Yes, Your Honor. I'm sorry.

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1 On that footnote six, Dr. Folwell, does it end at "in
2 producing other" that seems to kind of trail off there?

3 DR. FOLWELL: Well, I think the footnote
4 continues
5 -- the footnote continues on to the next page. That's
6 when we were still using typewriters.

7 MR. CARSWELL: The note on the next page. It
8 looks like footnote seven, so I just want to be sure we
9 have all of six.

10 DR. FOLWELL: To tell you the truth, right
11 now, as I look at it, it appears that on page 11 of this
12 copy that I brought with me, it wasn't all copied to
13 begin with.

14 MR. CARSWELL: Okay. So we don't have all of
15 footnote six.

16 DR. FOLWELL: That's correct. It's not there.

17 ADMINISTRATIVE LAW JUDGE: So it's -- it just
18 stops where it stops, even on the best copy we've got
19 here?

20 DR. FOLWELL: Yes.

21 ADMINISTRATIVE LAW JUDGE: Okay.

22 DR. FOLWELL: Exhibit 27 appears to be correct
23 as copied. Exhibit 29, the only relevant part to that
24 exhibit -- find it -- is from page 17 through 32.

25 ADMINISTRATIVE LAW JUDGE: And let's go off

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1 record while you compare those.

2 ***

3 [Off the Record]

4 [On the Record]

5 ***

6 ADMINISTRATIVE LAW JUDGE: Back on record at
7 1:39. Dr. Folwell, with regard to Exhibit 29?

8 DR. FOLWELL: It appears to be -- the relevant
9 pages of 17 through 32 were copied.

10 ADMINISTRATIVE LAW JUDGE: All right. Back to
11 Exhibit 28, is there anyone who objects to my allowing
12 the record copy to be the most recently made copy which
13 has the last line of the footnote difficult to read on
14 page 11? All right, there's no objection, so Dr.
15 Folwell, you may take with you the documents that you
16 brought with you and we'll make do with those copies of
17 them.

18 DR. FOLWELL: Thank you.

19 ADMINISTRATIVE LAW JUDGE: You're welcome.
20 Now I realize you've just been handed them, so I'll
21 defer the voir dire examination of the witnesses to
22 these for a little bit later in this process. Dr.
23 Hinman, did you have additional questions for Dr.
24 Folwell?

25 DR. HINMAN: Yes.

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1 ADMINISTRATIVE LAW JUDGE: You may proceed.

2 DR. HINMAN: Dr. Folwell, I'm going to re-ask
3 the question I asked earlier, because I found the quote.
4 It's actually not in the paper, but in the 1981 letter,
5 which is on page 13 of your report. I'm just going to
6 read the quote here, then ask you to comment on that.
7 "The marketing system is more stable in terms of having
8 a reliable supply as a result of the order. Facing this
9 risk, the cost of marketing hops have been less, which
10 aids in the overall efficiency of the hop industry." My
11 question to you is if you could just explain in a bit
12 more detail how the cost of marketing hops has been less
13 and the way in which that aids the efficiency of the
14 industry, in your view?

15 DR. FOLWELL: Basically, with a more stable
16 supply and the fact that inventories at that particular
17 point in time were not building up, there was less
18 waste. Also, you've got to take into consideration the
19 cost of holding inventories and by overall efficiency,
20 I'm referring to the cost associated with the marketing
21 of the hops.

22 DR. HINMAN: In terms of viewing the proposed
23 order in terms of -- you said that you can view it terms
24 of its total costs, in terms of its total benefits,
25 would you be able to say to the extent to which you

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1 believe the total benefits exceed the total costs of
2 implementing on order such as the one proposed?

3 DR. FOLWELL: Well, I think I can state
4 unequivocally that the benefits will outweigh the cost.
5 To quantify those here would be next to impossible.

6 DR. HINMAN: I think that concludes my
7 questioning. Thank you.

8 ADMINISTRATIVE LAW JUDGE: Thank you, Dr.
9 Hinman. Any other questions from representatives of the
10 United States Department of Agriculture? Ms. Finn?

11 MS. FINN: Thank you. I have one question,
12 Dr. Folwell. I would like to ask you your opinion on
13 this. In order for a future marketing order for hops to
14 be effective, do you believe it's important that all
15 domestic production be included and the regulated area?

16 DR. FOLWELL: I think it would be highly
17 desirable. The -- I think I'll just leave my answer to
18 that. I think it would be highly desirable because as I
19 indicated earlier, alpha is alpha at times in terms of
20 the beer industry and I think having both the aroma and
21 high alpha hops would be very desirable.

22 MS. FINN: Would that also extend to as far as
23 all of the states that produce hops?

24 DR. FOLWELL: Yes. I was going to add, I've
25 heard California mentioned here. I'm not sure if

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1 there's still hop yards left in California.

2 MS. FINN: Okay. Thank you.

3 ADMINISTRATIVE LAW JUDGE: Are there any other
4 questions from the USDA? None? Now, I'd like to open
5 the field for questions from anyone. Additional
6 questions for Dr. Folwell before we go on to the issues
7 of the three exhibits that have just been distributed.
8 Mr. Monahan?

9 ***

10 REDIRECT EXAMINATION

11 BY MR. MONAHAN:

12 Q. Thank you, Your Honor. Dr. Folwell,
13 there was some question on cross-examination about what
14 would happen, what hypothetically to the United States
15 hop growers market here and I want to ask if you know
16 what happened to US hop growers' market share, if
17 anything, under the old order?

18 A. My recollection, without doing the actual
19 calculations, is it either remained stable or slightly
20 increased.

21 Q. Do you have any knowledge or familiarity
22 with what has happened to the United States market share
23 in the last 10 years?

24 A. My general impression is that the market
25 share that the US industry holds is declining.

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1 Q. Is there any reason to think that it
2 wouldn't continue to decline, even if there is no
3 marketing order?

4 A. Not really.

5 Q. On the issue, again, of market share. Do
6 you know how many of that long list of nations that are
7 apparently now qualified as hop producing nations, how
8 many of those actually export hops?

9 A. The major exporters, of course, are
10 number one, Germany. The -- I can look it up, possibly
11 here. The major importers into this country under the
12 old order were, at least, West Germany, Yugoslavia,
13 Czechoslovakia, Poland, and others. Since then, China
14 has entered into the trade flow. And there could be
15 others.

16 Q. Just from a basic economic principle, or
17 standpoint, Doctor, if another country is able to bring
18 hops to market for less than it costs American hop
19 growers to produce that hop, isn't the loss of market
20 share going to be inevitable with or without a hop
21 marketing...

22 A. That's correct.

23 Q. Does it make any economic sense to try to
24 preserve market share at the expense of profit?

25 A. No.

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1 Q. Have other industries tried that?

2 A. Not that I'm aware of and existed in the
3 long run. They eventually went out of business.

4 Q. You were asked some questions by one of
5 the attorneys about this list of buyers, whether it's
6 four or perhaps higher. And there were some questions
7 about or rather, representations made about the
8 Anheuser-Busch Company. Do you know -- which I'll refer
9 to as AB, if you don't mind -- does AB buy super alpha
10 hops?

11 A. They might someplace in the world. My
12 understanding is currently they buy primarily aroma hops
13 here in the US.

14 Q. Do you know which variety of aroma hops?

15 A. Willamettes, I believe.

16 Q. Do you know what percentage of US hop
17 production is comprised of the Willamette variety?

18 A. I could look it up. It's a fairly high
19 percentage.

20 Q. I'm going to ask you to assume that it's
21 about 15 percent.

22 A. Right.

23 Q. Okay. I'm also going to ask you to
24 assume that 90 percent of the Willamette variety is
25 purchased by Anheuser-Busch? You were asked a number of

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1 questions about whether this type of scenario with these
2 number of buyers in the market is indicative of a
3 competitive market and I would ask you, Doctor, if there
4 is a variety comprising 15 percent of US production, and
5 if there's one purchase buying 90 percent of that
6 variety, is that indicative of a competitive market?

7 A. It's not, in my opinion.

8 Q. Mr. Moody asked you questions about
9 waste, what constitutes waste in the American hop
10 industry. In your opinion, from an economic standpoint,
11 does it constitute waste of a product to sell it out of
12 inventory at less than the cost of production?

13 A. Well, it's an economic waste in the sense
14 that no firm or operation can continue to do that
15 forever.

16 Q. Do you have an opinion as to whether
17 there was waste under the old order?

18 A. No. The only opinion I would have in
19 relation to the old order was that many of the hops that
20 were sold out of the reserve pool, their quality had
21 deteriorated over time. They were basically not worth
22 much money to a major brewer, mostly to the home -- the
23 person making beer at home.

24 Q. There's been some testimony -- and I'll
25 have to make representations to you, because you weren't

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1 in Portland last week. Some testimony that the hop
2 industry at this window in time is somewhat in balance,
3 at least in part because of a crop failure in Germany.
4 I would ask you, Doctor, in the absence of a hop
5 marketing order, would you reasonably anticipate this
6 current state -- supposed state of balance to continue?

7 A. I'm not so sure if I agree with the
8 statements that it's imbalanced to begin with, because
9 the level of stocks has continually increased, at least
10 over the last three to four years and it's having a
11 detrimental effect upon the price level. Whether or not
12 it's going to continue will depend upon how the order's
13 administrated and the decisions of the administrative
14 committee.

15 Q. My question, sir, is in the absence of an
16 order?

17 A. Well, in the absence of an order, more
18 than likely because of the nature of the inputs used in
19 hop production. Any time a hop producer out here who
20 has idled his yard or her yard sees a possibility of
21 utilizing those resources, they will probably overreact
22 to the price signal in the market place and possibly
23 over produce.

24 Q. Has that been the history and the
25 experience of the hop industry, sir?

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1 A. I would say so.

2 ***

3 MR. MONAHAN: Your Honor, those are all the
4 questions I have. I believe Mr. Roy has a question.

5 ADMINISTRATIVE LAW JUDGE: Thank you, Mr.
6 Monahan. Mr. Roy?

7 MR. ROY: Thank you, Your Honor. Dr. Folwell,
8 you know -- since you worked with the old marketing
9 order and in your testimony you indicated that the HAC
10 policy committee overestimated demand and underestimated
11 supply. Is that correct?

12 DR. FOLWELL: Correct.

13 MR. ROY: So if I remember right, the reserve
14 pool, which would be hops that were in excess -- that
15 were grown in excess of saleable quantity did not change
16 much through the years?

17 DR. FOLWELL: That's correct.

18 MR. ROY: So those excess hops went to...

19 DR. FOLWELL: Into the pool.

20 MR. ROY: Yeah, but after they came out of the
21 pool -- would that indicate that maybe some market share
22 has been gained?

23 DR. FOLWELL: Possibly, but I think a lot of
24 those hops were not necessarily sold to major brewers
25 around the world. But if they came out of the pool and

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1 were actually sold, it would indicate there is some
2 increase in market share. It might not have been among
3 major brewers.

4 MR. ROY: Yeah. Okay, thank you.

5 ADMINISTRATIVE LAW JUDGE: Thank you, Mr. Roy.
6 Are there any additional questions from anyone before we
7 get -- would you come forward to the microphone, please
8 -- before we get into the questions about the three
9 exhibits. Thank you. I know we've taken away your
10 podium. I hope there's enough table space there.

11 MR. CHANDRAMAZUMDAR: There is.

12 ADMINISTRATIVE LAW JUDGE: Do you want a
13 chair? You've got a chair, too. This is great.

14 MR. CHANDRAMAZUMDAR: I'm all set and I'm
15 Chandramazumdar from the United States Department of
16 Justice, Antitrust Division. Good afternoon, Dr.
17 Folwell. How are you?

18 DR. FOLWELL: I'm just fine.

19 MR. CHANDRAMAZUMDAR: Is -- has there been any
20 new entry by hop dealers recently?

21 DR. FOLWELL: New dealers? I'm not really
22 sure, but I think there's possibly been some re-
23 organization, but the major dealers are, you know, still
24 -- or buyers, if you want to include them, are Haas and
25 Steiner and Anheuser-Busch, et cetera.

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1 MR. CHANDRAMAZUMDAR: And how easy would it be
2 for a new dealer to enter?

3 DR. FOLWELL: Well, if they're well
4 capitalized, there shouldn't be too much of a problem,
5 assuming that they have the skills and the ability to
6 develop markets for the hops.

7 MR. CHANDRAMAZUMDAR: So it's fair to say that
8 the barriers to entry are low?

9 DR. FOLWELL: For a dealer? No, I wouldn't
10 say that because of the amount of capitalization it
11 really takes to enter the industry.

12 MR. CHANDRAMAZUMDAR: How much capitalization
13 does it take?

14 DR. FOLWELL: That would depend upon the size
15 of the dealer and how many, you know, pounds of alpha or
16 hops that they were purchasing and what arrangements
17 they had with their contracts and how they would sell
18 them to the brewers.

19 MR. CHANDRAMAZUMDAR: For a small dealer?

20 DR. FOLWELL: Handling how many pounds?

21 MR. CHANDRAMAZUMDAR: Can you -- of alpha
22 acid?

23 MS. FINN: Well, I think what you --
24 basically, what you'd have to do is just about take the
25 price at which the alpha acid is being priced at and

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1 they're valued at and multiply it times the amount of
2 pounds or the volume he wants to deal with and add on to
3 that the cost of doing business and at least for one
4 year you better have access to capital for that because
5 most agricultural producers I know want to be paid for
6 their crop in the year in which they produce it.

7 MR. CHANDRAMAZUMDAR: So I would need access
8 to capital in order to forward contract with growers?

9 DR. FOLWELL: If you're receiving the hops
10 from their actual production, yes.

11 MR. CHANDRAMAZUMDAR: And are there any other
12 entry barriers?

13 DR. FOLWELL: I'm sure there are, because
14 there tends to be relationships established within the
15 industry between brewers and dealers and the variety of
16 hops that the different brewers want.

17 MR. CHANDRAMAZUMDAR: And can you -- stepping
18 back, can you quantify how difficult it would be to
19 develop these relationships?

20 DR. FOLWELL: I think it would be extremely
21 difficult because, you know, the major brewers, they
22 probably account for the vast majority of the hops that
23 are being purchased both here domestically and from
24 international sources and it would be extremely costly
25 to try and represent all these micro-breweries that we

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1 have around the US today. I mean, that would not be a
2 very cost-effective way of being a dealer.

3 MR. CHANDRAMAZUMDAR: Turning to the micro-
4 breweries, if I'm a micro-brewery apparently purchasing
5 from a dealer such as Steiner or Haas, how difficult is
6 it for me to go in direct contract with a grower?

7 DR. FOLWELL: I assume that you could do it.
8 I mean, I don't see any major barriers other than the
9 fact that perhaps the growers themselves do not want to
10 deal in small lots with these micro-brewers. I mean,
11 most of these -- at least when we used to bail the old
12 aroma hops, a bail was 200 pounds and that makes a lot
13 of beer. When you're only putting two-tenths of a pound
14 or less in for 31 gallons of beer.

15 MR. CHANDRAMAZUMDAR: Is it your conclusion
16 that the dealers have market power?

17 DR. FOLWELL: I believe so.

18 MR. CHANDRAMAZUMDAR: And is that conclusion
19 based on the fact that there are four dealers,
20 currently, in the market?

21 DR. FOLWELL: Well, four or six, whatever.
22 Whichever number you want to use. And I think also that
23 the -- in one of the exhibits that I have read, there
24 were statements made which indicated they had market
25 power, that they weren't quite sure what they were going

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1 to do in terms of forward contracting until the findings
2 of this hearing were released.

3 MR. CHANDRAMAZUMDAR: And what else?

4 DR. FOLWELL: And what else?

5 MR. CHANDRAMAZUMDAR: What else goes into your
6 conclusion?

7 DR. FOLWELL: About the market power...

8 MR. CHANDRAMAZUMDAR: Market power.

9 DR. FOLWELL: ...dealers? Anything I say to
10 you right now would be hearsay and I don't know if you
11 want that or not, but basically, you know, I've heard
12 that the largest brewer in the world was in the
13 Northwest here talking about this proposed marketing
14 order and did not have very positive statements to make
15 about it. That's -- you know, and that was hearsay.

16 MR. CHANDRAMAZUMDAR: Okay. I understand that
17 are both for contracts and spot hops. Do forward
18 contracts serve a different function than selling on the
19 spot market?

20 DR. FOLWELL: Do they serve a different
21 function? The contracting, you know, provides the
22 grower with an assured market outlet and an assured
23 price which we talked about earlier, which means I can
24 go to my banker and show him, you know, my books and
25 basically say, look, I want to borrow this much money

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1 and I have the ability to service this debt loan. For
2 the brewer, yes, it has advantages. It assures the
3 brewer of the variety and the quality of hops they want
4 for a product that they're producing out there for the
5 consumer and the brewers go to great lengths to
6 establish a product with certain characteristics which
7 their consumers would like to have. So there's
8 advantages on both sides.

9 MR. CHANDRAMAZUMDAR: When I go to my banker,
10 do I need a forward contract? Do those forward
11 contracts enable me to decide how I'm going to invest in
12 infrastructure?

13 DR. FOLWELL: Since I am a banker and serve on
14 a board of directors, I can tell you that when
15 agriculturalists come to us for loans that, in fact, we
16 want them to demonstrate to us that they have the
17 ability to service the debt load that they're going to
18 take on. So the contract is very important. If you're
19 planting something without a contract, it's basically
20 being planted on a speculation basis and it's much more
21 risky.

22 MR. CHANDRAMAZUMDAR: And what function does
23 the spot market in hops serve?

24 DR. FOLWELL: Well, basically, it's an outlet
25 for, you know, that quantity of hops which are not under

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1 contract. It provides a way of sort of balancing what
2 was produced with what is being demanded in the market
3 place and it's not surprising to see a spot market price
4 vary more than what you'll ever see under contracts.

5 MR. CHANDRAMAZUMDAR: And when spot prices
6 increase, dealers or brewers or growers who have an
7 inventory release that inventory?

8 DR. FOLWELL: Some do, but you have to realize
9 that the amount of spot hops, at least historically in
10 this country have been a relatively small proportion.
11 Those who have inventory and feel that they can profit
12 from releasing the stocks will do so.

13 MR. CHANDRAMAZUMDAR: And conversely, when
14 spot price are low, people increase their inventories?

15 DR. FOLWELL: Growers? Brewers might increase
16 their inventories slightly, growers don't necessarily
17 like to increase their inventories because they've got
18 an investment in terms of the cost of production plus
19 the cost of carrying those inventories, so growers are
20 not very anxious to increase their inventories.

21 MR. CHANDRAMAZUMDAR: In your statement, what
22 I believe has been marked by the court as Exhibit 26, in
23 the first paragraph you state that "in the past, the
24 stability" -- I'll give you a chance to turn to it. Do
25 you have it? You basically say that "in the past the

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1 stability has been demonstrated by the percent of hops
2 sold or contracted ahead. This percentage has been
3 slowly declining." Can you explain what you mean by
4 slowly declining?

5 DR. FOLWELL: There was another exhibit which
6 I saw, which I believe was a document created by Hop
7 Growers of America. It was entitled almost the same
8 title I have on this paper. Something related to the
9 need for a federal marketing order. Historically, the
10 percentage of hops that were contracted as harvest was
11 approaching, as we're coming closer and closer to
12 harvest was usually 90 percent or higher. I believe in
13 that Hop Growers of America report in which they conduct
14 a survey, I believe it's down to 66 percent or something
15 of that nature. I don't have the exhibit in front of
16 me.

17 MR. CHANDRAMAZUMDAR: Turning your direction
18 to another exhibit, Exhibit 27, your paper...

19 DR. FOLWELL: Correct.

20 MR. CHANDRAMAZUMDAR: ...which is titled "The
21 US Hop Industry and the Volume Control Provision of the
22 US Federal Hop Marketing Order." I'd like to direct
23 your attention to your summary statement, which I
24 believe is at page 16.

25 DR. FOLWELL: Yes.

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1 MR. CHANDRAMAZUMDAR: And you state "as a
2 result, it can be partially concluded that the HAC has
3 not unduly used its market power in restricting the
4 quantity of hops available to the market from domestic
5 production." Did I read that correctly?

6 DR. FOLWELL: Correct.

7 MR. CHANDRAMAZUMDAR: When you use the term
8 unduly restrict, doesn't that mean that the HAC did
9 restrict?

10 DR. FOLWELL: They set the saleable percentage
11 every year. There could've been individual producers
12 out there who wanted to produce or market, I should say,
13 market more pounds of hops than what the saleable was
14 suggesting they do. But that doesn't necessarily mean
15 that they were restricted in what they were -- what they
16 could produce.

17 MR. CHANDRAMAZUMDAR: The amount marketed?

18 DR. FOLWELL: The amount marketed was
19 regulated under the old marketing order.

20 MR. CHANDRAMAZUMDAR: And isn't the amount
21 marketed the same as the quantity of hops available to
22 the market?

23 DR. FOLWELL: That plus the stocks that are
24 being held by brewers and dealers and growers.

25 MR. CHANDRAMAZUMDAR: But those stocks aren't

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1 available for sale on the market?

2 DR. FOLWELL: As far as I know, they were.
3 Some of the stocks are actually being held by brewers
4 and dealers. They'd already been sold by the growers.

5 MR. CHANDRAMAZUMDAR: Okay. In that paper,
6 you did not use any data past 1980.

7 DR. FOLWELL: Correct.

8 MR. CHANDRAMAZUMDAR: And this morning you
9 testified that the instability after 1980 was due to
10 market conditions, not the marketing order. And isn't
11 it...

12 ADMINISTRATIVE LAW JUDGE: Just let me get
13 that on record. Doctor, you nodded your head yes, is
14 that so?

15 DR. FOLWELL: I'm understanding what he said.

16 ADMINISTRATIVE LAW JUDGE: Okay. He's with
17 you. You may continue.

18 MR. CHANDRAMAZUMDAR: Okay. And isn't it
19 possible that the stability that you perceived was due
20 to the marketing order was, in fact, due to current
21 market conditions?

22 DR. FOLWELL: Current market conditions...

23 MR. CHANDRAMAZUMDAR: Current market
24 conditions for the relevant period of your study and --
25 I'd like -- let me rephrase that. Is it possible that

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1 the stability that you observed was not due to the
2 marketing order but was, in fact, due to market
3 conditions?

4 DR. FOLWELL: You have to realize that the
5 saleable percentage, though, was a direct function of
6 the market conditions that was set by the HAC, so their
7 interpretation of the trends in the market and the
8 market conditions led to stability in terms of providing
9 and adequate flow of hops to the market.

10 MR. CHANDRAMAZUMDAR: You indicated that the
11 instability was due to -- after 1980 was -- it was also
12 due to market conditions. And shouldn't the HAC have
13 somehow taken into account those market conditions?

14 DR. FOLWELL: The HAC could only recommend to
15 the Secretary of Agriculture the saleable percentage
16 approximately 18 months ahead. And they could only
17 recommend it for one marketing year. They did not have
18 the tools at hand nor the authority under the existing
19 law to set the saleable percentage for more than one
20 market year.

21 MR. CHANDRAMAZUMDAR: Backing up a moment. If
22 market conditions were stable, you would expect that the
23 HAC would be able to accurately predict them? Or
24 predict the demand?

25 DR. FOLWELL: Well, fairly accurately.

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1 MR. CHANDRAMAZUMDAR: And in contrast, if
2 market conditions were not stable, the HAC would not be
3 able to accurately predict the demand?

4 DR. FOLWELL: The more variation in any supply
5 or demand component there is, the harder it is to
6 produce and as a matter of fact, the component that they
7 had the most difficulty in projecting in terms of the
8 overall accuracy was the foreign trade components, which
9 are as much political at times as they are economic in
10 nature.

11 MR. CHANDRAMAZUMDAR: So if market conditions
12 were stable, how can -- you would expect that the HAC
13 would be able to accurately predict them? Predict
14 demand?

15 DR. FOLWELL: Fairly accurately, and as a
16 matter of fact, the HAC did react to this crop failure
17 that's been alluded to many times today in the sense
18 that they raised the saleable percentage, I believe,
19 from something like -- I don't have the exact figures,
20 but something like from 107 up to 130 percent to try and
21 fill that void in the market that was created by the
22 crop failure in Czechoslovakia and Germany.

23 MR. CHANDRAMAZUMDAR: But that data's not
24 reflected in your paper, that's Exhibit 27. That period
25 of time?

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1 DR. FOLWELL: If, in fact -- I had to reread
2 this thing before, but if, in fact, it included the time
3 period through 1980, it would've.

4 MR. CHANDRAMAZUMDAR: Okay. This morning you
5 stated that the hop marketing order could generate
6 useful market information.

7 DR. FOLWELL: Yes, sir.

8 MR. CHANDRAMAZUMDAR: Can't useful market
9 information be generated without a hop marketing order
10 that has volume limitations?

11 DR. FOLWELL: It can be, but the typical
12 agricultural producer usually does not have the time nor
13 the expertise always to sit down and collect and
14 assemble such information. As a matter of fact, I
15 brought with me an example here which is approximately I
16 don't know how many pages here of statistics 13, 14, 15
17 pages of statistics that the HAC assembled quarterly and
18 in fact, the administration of the committee as well as
19 the statistical subcommittee and all member of the HAC
20 had opportunities to comment upon their interpretation
21 and what they thought was happening in the hop market,
22 not only in the US, but worldwide and I never saw -- I
23 have never experienced another industry where individual
24 growers had the information just handed to them in a
25 packet like that.

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1 MR. CHANDRAMAZUMDAR: But a committee could
2 certainly assemble that information and not administer
3 volume limitations.

4 DR. FOLWELL: That might be possible, but the
5 contacts that this federal marketing order had in Europe
6 and other places was invaluable.

7 MR. CHANDRAMAZUMDAR: But couldn't that
8 committee be established just to collect market
9 information and not administer volume limitations?

10 DR. FOLWELL: That's a possibility.

11 MR. CHANDRAMAZUMDAR: This morning you also
12 said that unless something happened someday this
13 industry's going to be extinct. Can you expand upon
14 this?

15 DR. FOLWELL: Well, when you drop from 211
16 down to
17 -- I've heard a number -- I have 70 in my report but
18 I've heard a number as few as 45 growers, you know,
19 independent growers are still left out here. It's
20 obvious to me that the trend is set there. Maybe the
21 word extinct is a little bit strong, but I could
22 basically see a time when we might be down to a dozen or
23 less hop growers even in my lifetime. The question was
24 asked to me earlier if somebody else can produce the
25 hops cheaper, isn't that where the brewers are going to

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1 turn? The answer is yes. I mean, our growers cannot
2 continue to produce hops at less than the cost of
3 production and stay in business.

4 MR. CHANDRAMAZUMDAR: And can you estimate
5 what volume these less than a dozen hop growers would
6 produce?

7 DR. FOLWELL: Oh, I would guess -- believe it
8 or not, probably someplace in the neighborhood of 45 to
9 50 million pounds.

10 MR. CHANDRAMAZUMDAR: So slightly less than
11 current production?

12 DR. FOLWELL: Probably.

13 MR. CHANDRAMAZUMDAR: Thank you.

14 ADMINISTRATIVE LAW JUDGE: Thank you, Mr.
15 Chandramazumdar. Mr. Carswell?

16 MR. CARSWELL: Yes. Dr. Folwell, earlier you
17 mentioned with respect the Willamettes that Anheuser-
18 Busch -- you said the world's largest brewer and that
19 would be Anheuser-Busch purchased, I believe you said 90
20 percent of the Willamettes?

21 DR. FOLWELL: I believe the person asking the
22 question stated that as the framework with which to
23 answer his question.

24 MR. CARSWELL: You concurred with that or...

25 DR. FOLWELL: I have no reason to disagree

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1 with it. Do I have actual statistics on it? No, I do
2 not.

3 MR. CARSWELL: What would be the significance
4 of that? Would you say then that we have market power
5 in the quote, unquote Willamette market and not put it
6 in quotes because I question the validity of the market
7 so defined, but a market from an antitrust standpoint.

8 DR. FOLWELL: If, in fact, you have a unique
9 demand for those Willamettes and everything and you're
10 buying 90 percent, I would say that you have some market
11 power.

12 MR. CARSWELL: Are you familiar with Anheuser-
13 Busch pricing to its growers for growers of Willamettes?

14 DR. FOLWELL: Not currently.

15 MR. CARSWELL: Considering your indication
16 that you would think that we would have market power,
17 would it surprise you if the growers, including some of
18 the proponents have already indicated on the record that
19 that pricing has been very fair and equitable from a
20 grower's standpoint?

21 DR. FOLWELL: It could be. I have no
22 knowledge of that.

23 MR. CARSWELL: Is it your understanding that
24 aroma hops are the type of hops for which a marketing
25 order is -- has been -- do you see the problem with

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1 aroma hops vis-à-vis alpha hops in the current economic
2 situation? For hop growers? Sorry.

3 DR. FOLWELL: Do I see the same problem for
4 the aroma growers as I do for the alpha...

5 MR. CARSWELL: Yes.

6 DR. FOLWELL: ...high alpha? Basically, I
7 think that the -- whether it's imbalanced or not, I'm
8 not in a position to judge that right now, but I think
9 it would be very easy for the aroma market to be
10 completely out of balance and more hops being produced
11 in that -- for those particular type of hops than was
12 really demanded by the market and we'll go through the
13 same cycle that we have been going through here with the
14 high alpha.

15 MR. CARSWELL: On the alpha side, do you see
16 -- and you've indicated before that that can be
17 established, I believe, that there are some -- there's
18 some number more than four buyers of alpha hops. Do you
19 see there being market power on the -- or monotony [ph]
20 power on the buy side for alpha hops?

21 DR. FOLWELL: You use the word monopsony [ph]
22 which means, you know, one. If you would use the word
23 oligopsony [ph], I'd probably agree with that statement.

24 MR. CARSWELL: Even if there were say, 10
25 buyers, you would still call that an oligopsony?

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1 DR. FOLWELL: I think that's getting down to
2 the point where the -- those buyers are very cognizant
3 of each other's behavior and they don't necessarily have
4 to exchange information or anything else like that, but
5 I think there is the opportunity to exercise market
6 power in those cases.

7 MR. CARSWELL: With respect to the Willamette
8 hops, why do you think that there's a certain amount of
9 Willamette hops grown in this country?

10 DR. FOLWELL: Because there's a demand for
11 them.

12 MR. CARSWELL: And if there was no demand for
13 them and if there was no agreement to grow those hops
14 for one or more brewers, do you think they would be
15 grown?

16 DR. FOLWELL: I think, in the very short run,
17 some of them would be grown. Eventually, if there was
18 no demand, no market, no price for them, that the
19 growers would eventually plow those out.

20 MR. CARSWELL: Are you familiar with any spot
21 market for Willamettes?

22 DR. FOLWELL: No. The spot market --
23 information on the spot market has almost disappeared
24 over the years since the USDA is not really recording
25 it.

1 MR. CARSWELL: So it would stand to reason
2 that nobody's going to grow Willamettes unless they have
3 somebody to buy them, is that correct?

4 DR. FOLWELL: I would hope so.

5 MR. CARSWELL: And they wouldn't have anybody
6 to buy them -- I'm sorry. They wouldn't grow them --
7 they would grow another hop if it was in their economic
8 interest to do so, to grow some other crop.

9 DR. FOLWELL: I would assume so.

10 MR. CARSWELL: It would seem to follow, then,
11 that it's -- that they must be getting a fair price for
12 those hops or they wouldn't grow them.

13 DR. FOLWELL: First of all, I don't know that
14 the price level of Willamettes is versus the cost of
15 production or anything, but as long as they're staying
16 in production and covering their -- at least their out-
17 of-pocket costs in the short run and hopefully all their
18 costs in the long run, they will stay in production.

19 MR. CARSWELL: Would it be a monopsonous [ph]
20 economic interest to drive the profitability of growing
21 the hops that the monopsonous needs, in the long run,
22 would it be a monopsonous interest to depress prices
23 which would affect quality of the hops and the supply of
24 hops?

25 DR. FOLWELL: Not unless that monopsonous

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1 could see some other supply of those particular hops.

2 MR. BARTON: Can we go off record a moment?

3 ADMINISTRATIVE LAW JUDGE: All right.

4 ***

5 [Off the Record]

6 [On the Record]

7 ***

8 ADMINISTRATIVE LAW JUDGE: All right, we went
9 off record at 2:19, it's still 2:19. We're back on
10 record.

11 MR. CARSWELL: Dr. Folwell, you mentioned
12 earlier that in response to a question from Ms. Finn
13 from USDA that you unequivocally, I believe you said,
14 thought that the benefits would outweigh the costs under
15 the marketing order.

16 DR. FOLWELL: That's true.

17 MR. CARSWELL: It's my understanding you
18 hadn't -- if I'm -- correct me if I'm mistaken, but I
19 thought from your testimony that you haven't really
20 studied the marketing order, is that...

21 DR. FOLWELL: You mean the proposed one?

22 MR. CARSWELL: Yes, sir, the proposed one.

23 DR. FOLWELL: I was answering that in relation
24 to what the state of the industry and what happened at
25 the termination of the last order.

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1 MR. CARSWELL: So you don't know what the
2 effect of the proposed marketing order, what effect that
3 would have?

4 DR. FOLWELL: If it's anything close to what
5 the last order was, I think the benefits would surely
6 outweigh the costs that would be associated with it. I
7 have observed over -- I know over 20,000 acres of hops,
8 hop yards being idle in the Northwest here and when you
9 consider the amount of investment per acre to establish
10 those yards and the fact that they have almost -- except
11 for the land -- have zero salvage value, that's a
12 misallocation of resources. And that's a cost to
13 society for doing that. It doesn't pay to raise wheat
14 in those hop yards.

15 MR. CARSWELL: You don't think it could be a
16 reflection of the development of super alphas?

17 DR. FOLWELL: The super alphas have
18 contributed to the overall problem, the Tomahawk, et
19 cetera, in the sense that this "new technology" through
20 plant breeding that's come into play here and the --
21 which it's contributed to the oversupply situation.
22 There's no doubt about it.

23 MR. CARSWELL: Well, you call it a problem,
24 but isn't it good for society if more alpha is produced
25 on fewer acres?

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1 DR. FOLWELL: It is in essence, unless
2 producers have reacted and gone out and planted a lot of
3 hop yards that then are no longer in use and the land is
4 sitting idle, all the investment is lost. That's what
5 I'm considering the cost.

6 MR. CARSWELL: Wouldn't it be a better use of
7 that land to grow something else on the land?

8 DR. FOLWELL: Well, right now in the Yakima
9 Valley there aren't too many good alternatives.

10 MR. CARSWELL: I'm not -- no expert on the
11 Yakima Valley and I certainly don't mean to...

12 DR. FOLWELL: I know...

13 MR. CARSWELL: ...belittle the problem, but if
14 enough hops are being grown on land so that there are
15 thousands of acres of land with hop development that's
16 not being used and it's not needed, wouldn't it make
17 sense from an economic standpoint to grow something else
18 on that land? Such as apples, for example?

19 DR. FOLWELL: No.

20 MR. CARSWELL: Maybe not apples.

21 DR. FOLWELL: Try another one.

22 MR. CARSWELL: Something else...

23 DR. FOLWELL: Yes...

24 MR. CARSWELL: ...other than hops?

25 DR. FOLWELL: ...that's true. But one of the

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1 problems with a hop yard, once it's idled, there's a
2 tendency to leave those poles and wires out there and I
3 can take you by I don't know how many hop yards right
4 now where the land is actually sitting idle. It's not
5 being used. It's not CRP [ph] or anything else, so it's
6 just -- it's there. It's idled. The growers don't have
7 an alternative to it until they go in to the expense of
8 removing those poles and wires.

9 MR. CARSWELL: So do you think that under a
10 hop marketing order they'll plan to bring those back?

11 DR. FOLWELL: I have no -- I can't predict
12 that. That depends upon how well the marketing order is
13 administered and their philosophy about trying to
14 increase their market share.

15 MR. CARSWELL: Well, if there's an oversupply,
16 why would they ever bring more land back into
17 production?

18 DR. FOLWELL: Because if in fact this order is
19 initiated, I would expect initially that there will be
20 some producers who have historically produced hops not
21 produce them and as a matter of fact, I would almost
22 suggest here that there will probably be a lot more base
23 allocated out than will ever be used. And eventually,
24 once the market has -- I don't want to use the word
25 balanced -- equivocally come back into -- I'll use the

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1 word balance, I guess, here between supply and demand.
2 Then I think you'll start to see some resources flow
3 back into hop production. Now, whether it's the same
4 existing yards out there with the poles and the wire,
5 that's anybody's guess. Perhaps it will be a new yard.

6 MR. CARSWELL: Would you expect the net to
7 increase in hop production from today to that point in
8 the future where these farms may come in?

9 DR. FOLWELL: Not initially, I don't expect
10 it. As a matter of fact, if anything, I see possibly
11 some decline in terms of the amount of hops being
12 produced in order to bring this market back into balance
13 overall in terms of the amount of alpha produced and the
14 demand for it. But eventually, assuming that the beer
15 consumption rises and we increase our market share
16 overseas, then I -- there is the possibility of some of
17 these families who've been in hop production for decades
18 coming back to the hop production.

19 MR. CARSWELL: Well, if we decline production
20 I don't see how we would -- I guess you're not saying
21 initially we would increase market share overseas if
22 we're declining production, is that correct?

23 DR. FOLWELL: Probably not. Not initially.
24 It's going to take time to work at that and develop
25 those markets.

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1 MR. CARSWELL: But you would say that long-
2 term we'll have initial decline in production with an
3 eventual expansion of production?

4 DR. FOLWELL: Well, I think you're going to
5 see production at least stay where it's at and not
6 increase. Now, how much it might go down or something
7 is up to the individual producers in their decision
8 making, but eventually I think if the market is
9 effective and they develop markets overseas, increase
10 their market share, then in fact some of these families
11 that have gone out of production could come back. It's
12 a very expensive operation to get back into, though.

13 MR. CARSWELL: But I don't understand how you
14 expand production under the marketing order.

15 DR. FOLWELL: I'm not -- how do I expand
16 production?

17 MR. CARSWELL: Yes, how do you expand --
18 production be expanded?

19 DR. FOLWELL: If, in fact, the market shares
20 start increasing both domestically replacing imported
21 hops as well as selling more hops overseas, I would
22 assume that there would be some positive impact upon
23 prices and with that positive impact on prices, you're
24 going to see producers more willing to produce hops.

25 MR. CARSWELL: And though that increase in

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1 prices would have to take into account for some growers,
2 at least, an increase in cost based on buying base,
3 correct?

4 DR. FOLWELL: If they didn't have sufficient
5 base to begin with, but I think initially that the base
6 itself, under a proposed new marketing order -- and I
7 think this has been experienced under the mid order has
8 very, very little value to begin with. So for somebody
9 to enter at the initiation of an order or shortly
10 thereafter, that this increase in cost of production is
11 not going to be significant.

12 MR. CARSWELL: Even though it was up to \$2 a
13 pound under the previous order?

14 DR. FOLWELL: And when -- that's also when you
15 saw the price almost increase tenfold.

16 MR. CARSWELL: And you're basing -- I'm sorry.
17 You're stating this even though you don't know how,
18 under the proposed order, the allotment would be set and
19 you don't know how much it would take to cut for the
20 saleable -- of the saleable quantity to cut overall
21 production?

22 DR. FOLWELL: I have not made those
23 calculations.

24 MR. CARSWELL: Thank you.

25 ADMINISTRATIVE LAW JUDGE: Thank you, Mr.

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1 Carswell. Mr. Moody, do you have any additional
2 questions at this time?

3 ***

4 REXCROSS EXAMINATION

5 BY MR. MOODY:

6 Q. Yes. I'll just ask a couple. You
7 indicated that -- in your paper that you thought that
8 alpha was basically alpha and that German hops were a
9 perfect substitute for US-grown hops?

10 A. Of the same variety, yes.

11 Q. When you say variety, do you mean like
12 the CTZ [ph] variety, the substitute for CTZ or the
13 alpha, any alpha's as good as any other alpha?

14 A. No, not alpha. In terms of people in the
15 brewing industry, there has always been a great concern
16 about the variety of hops that they use and even though
17 hops represent a very minute amount in terms of the
18 total cost of beer production, at least my experience
19 has been, under the previous order, is that everybody
20 from the president and CEO on down wants to go down to
21 the loading dock and rub those hops in their hands and
22 smell them and see what odors, flavors, et cetera, are
23 possible from them, so it's hard to say. If it's
24 exactly the same variety, yes, there are substitutes and
25 assuming they have the same brewing characteristics.

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1 Q. All right. And what in economic terms
2 does it mean -- if one is the substitute for the other,
3 doesn't that mean that an increase in price in one will
4 cause consumption to shift to the other?

5 A. Correct.

6 Q. Now, we export hops as well, right?

7 A. Yes.

8 Q. And would the same be true -- you could
9 say in reverse that the hops we export are also
10 substitutable for by other hops produced elsewhere in
11 the world.

12 A. That's correct.

13 Q. So if our hops increased in price in the
14 world market that it would be expected that brewers
15 would switch to a substitute.

16 A. Assuming a price in the other -- from
17 other sources did not increase, that's correct.

18 Q. All right. So given that US industry now
19 is somewhere between 25 and 30 percent of the world
20 market, at least with respect to the alpha varieties of
21 hops, they are substitutes both as to imports and
22 exports. How is it you expect to increase the price of
23 US hops in the long run given the ease of substitution
24 with hops produced elsewhere?

25 A. By increasing the demand. I've watched
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1 the hop industry here go to great lengths to try and
2 persuade brewers not only domestically, but from other
3 countries to use their hops.

4 Q. All right, I'm sorry. You're going to
5 have to walk me through that a little bit. You want to
6 increase the demand for US-grown hops?

7 A. Yes.

8 Q. But I thought -- well, since US-grown
9 hops are substitutes for German hops, how do you expect
10 to increase the demand for US-grown hops?

11 A. Well, first of all, there's going to be a
12 very high correlation between the price movement of hops
13 in this country, as well as in Germany. Part of this
14 increasing of demand comes from a marketing strategy
15 that the industry might employ in terms of persuading
16 brewers to use their hops.

17 Q. Well, is there something different under
18 a marketing order that I maybe have missed. I thought
19 that US growers, with or without a marketing order are
20 pretty interested in getting brewers to use their hops.

21 A. They are, but the overall collective
22 action of the growers here to put forth a noticeable
23 effort to attract brewers to use their hops is really
24 not there unless they have some type of organization or
25 umbrella. And I'm not saying that all of this occurs

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1 under a federal marketing order. In fact, a lot of it
2 occurs with other organizations that are associated with
3 the hop industry. They all work together.

4 Q. Don't the Hop Growers of America already
5 have sort of a promotional cheerleading?

6 A. Yes, they do.

7 Q. But how would a marketing order add to
8 that?

9 A. Only in the sense that all the growers
10 are sort of under one umbrella and working together,
11 otherwise you often have the vision within industries
12 and one faction pulling against the other.

13 Q. Do you expect the price of US hops, then,
14 to increase and the price of German and Chinese hops to
15 remain the same?

16 A. No, I didn't say that. I said there's a
17 high correlation between the prices in the US and other
18 places for similar-quality hops.

19 Q. All right, did you expect the other major
20 hop producing regions of the world to sort of follow the
21 US lead and join the US cartel in some way?

22 A. Cartel?

23 Q. Or marketing order?

24 A. The arrangements for selling hops in
25 other countries I think is a little bit different than

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1 what exists around here. But I don't expect them,
2 necessarily, to form a marketing board, let's say, in
3 another country which is common in some hop producing
4 countries such as Australia.

5 Q. Okay, then. I apologize for maybe
6 beating a dead horse here, but I just -- I'm having a
7 hard time reconciling your testimony that there's --
8 that are substitutes and your assumption you increase
9 the price of the US hops without affecting the prices of
10 foreign-grown hops. I'm afraid I just don't understand
11 that. If you could walk me through a little bit. How
12 could they be expected to do that?

13 A. Well basically, any producer of a
14 product, whether it be a hop grower here or Anheuser-
15 Busch or Coors, all try to develop some loyalty towards
16 their products. And it is, in fact, through marketing
17 efforts you can do that, then there is the possibility
18 of possibly capturing a larger market share, a larger
19 demand for US hops. There's no doubt that the prices
20 among the US and other producing countries are highly
21 correlated and are going to move together for the same
22 quality product.

23 Q. Okay. But is there some feature to the
24 marketing order other than its ability to restrict
25 supply that will engender some loyalty by buyers of US

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1 hops?

2 A. Not that alone, no, it will not. And
3 they're not attempting to restrict supply. They're
4 trying to create an orderly marketing situation.

5 Q. I thought -- wasn't the purpose of the
6 marketing to restrict supply?

7 A. Perhaps we're playing with words here,
8 but the provision, the allotment provision, only allow
9 for setting the saleable percentage, which was the
10 amount of hops available to the market from US
11 production.

12 Q. Right and as cultural economists use the
13 term, isn't that a restriction of supply?

14 A. Assuming that other people are willing to
15 supply more, I suppose you could interpret it that way,
16 but I can also take your words of restriction on supply
17 and interpret that as means I'm trying to restrict
18 production, which is against the law under the federal
19 marketing order.

20 Q. No, I'm just talking restriction on
21 supply and reaching the market.

22 A. That's what a producer allocation
23 provision provides for an orderly flow of hops to the
24 market given what the demand is.

25 Q. All right. So then the purpose of this
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1 order, I suppose, is to restrict the supply of US hops
2 reaching the market?

3 A. The purpose of this order in -- at least
4 in my interpretation of it is to create an orderly
5 marketing process.

6 Q. Right. By restricting supply.

7 A. I'm not going to say that.

8 Q. Okay. Then, how do you expect, without
9 restricting supply, how do you expect to increase the
10 price of US hops?

11 A. By providing a more orderly supply and
12 through possibility of the industry becoming more
13 focused upon marketing programs.

14 ***

15 MR. MOODY: Like -- well, is there -- okay.
16 Let me get back to my other questions. Is there
17 something I'm missing about the proposed marketing
18 order? I thought it was pretty much a -- you keep
19 referring to other features or other -- something other
20 about the order that will increase demand for US hops
21 besides the saleable percentage provisions. Is there
22 something I'm missing?

23 MS. DESKINS: Your Honor, at this point, I
24 think I need to object. I think the witness has
25 answered Mr. Moody's question and at this point I think

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1 it's just badgering the witness.

2 ADMINISTRATIVE LAW JUDGE: The objection is
3 noted. If I might just jump in, Mr. Moody. Dr.
4 Folwell, are you aware of anything else in the marketing
5 order besides the balancing of supply and demand that
6 might contribute toward increasing the price?

7 DR. FOLWELL: No, Your Honor.

8 ADMINISTRATIVE LAW JUDGE: All right. Mr.
9 Moody?

10 MR. MOODY: All right. So the only price
11 increasing potential in the marketing order is its
12 ability to restrict supply reaching the market, is that
13 correct?

14 ADMINISTRATIVE LAW JUDGE: That
15 mischaracterizes the witness's testimony. Do you want
16 to talk about restricting the supply when demand is low
17 and increasing the supply when demand is high? Is that
18 what you want to ask about?

19 MR. MOODY: Well, Your Honor and Dr. Folwell,
20 what I'm trying to do is I'm -- maybe you can answer
21 this. I'm trying to reconcile two parts of your
22 testimony. One opts for substitutes in the world
23 market, both imports and exports based on price. And
24 two, that some feature in this marketing order will
25 increase the price of US hops in the long run. I'm

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1 trying to reconcile those two notions. They seem, in
2 economic terms, mutually inconsistent.

3 DR. FOLWELL: The orderly flow of hops to the
4 market and an assured supply would possibly increase the
5 demand for US hops. It might also, through the
6 administrative committee and by setting the saleable
7 percentage give growers direction in terms of their
8 decision making on what to produce. And by having
9 better market information overall, in terms of having
10 all of the statistics and market information available
11 on their decision making, I would assume that these
12 growers would be making better decisions in terms of
13 what varieties to produce and in what quantities.

14 MR. MOODY: Well, is there some information
15 that would be provided under the marketing order that's
16 not presently available to them?

17 DR. FOLWELL: I think for the average grower,
18 yes. There's a lot of information that will be provided
19 to the growers that they will not make the time and
20 effort or put forth the time and effort right now to
21 collect and analyze.

22 ***

23 BY MR. MOODY:

24 Q. Because -- between HGA and USDA and the
25 states, there's quite a bit of information available

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1 already and information they get from the brewers and
2 dealers.

3 A. There is, there is.

4 Q. And what else would be provided under the
5 marketing order?

6 A. Contacts with other organizations
7 overseas in terms of providing their interpretation of
8 the trends in the market, that's an example.

9 Q. Isn't that function presently being
10 performed, essentially, by the dealers?

11 A. Yeah. I suppose you could say that, but
12 there's always, you know, when I'm out to buy something
13 I try to buy at the lowest price and if I'm out to sell
14 something, I try to sell it at the highest price.

15 Q. And isn't -- organizations in the
16 industry like now, like HGA and Yakima Chief and groups
17 like that provide that type of coordinating function.

18 A. I think they do provide some of it, but I
19 don't think it's necessarily supplied at the level of
20 sophistication that I observed under the past federal
21 marketing order.

22 ***

23 MR. MOODY: All right. Thanks very much, Dr.
24 Folwell.

25 DR. FOLWELL: Thank you.

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1 ADMINISTRATIVE LAW JUDGE: Mr. Moody, HGA?

2 MR. MOODY: Hop Growers of America.

3 ADMINISTRATIVE LAW JUDGE: Hop -- okay. Good.

4 Thank you. All right. If there's no objection, I'd
5 like now to go to the three exhibits that we have not
6 yet admitted into evidence and ask if anyone would like
7 to voir dire Dr. Folwell about Exhibit 27 or Exhibit 28
8 or Exhibit 29? And I'm aware that you haven't had a lot
9 of time to have them in your hands, but knowing that
10 this is his last day, probably, with us we need to get
11 to these issues. Would it help if I took a 10-minute
12 break now about that? Does anyone request a 10-minute
13 break right now about that? All right, let's take a --
14 just a 10-minute comfort break then please be back ready
15 to go at 2:51.

16 ***

17 [Off the Record]

18 [On the Record]

19 ***

20 ADMINISTRATIVE LAW JUDGE: We're back on
21 record at 2:52. During the break a number of people
22 were looking for coffee, hot water for tea in the back
23 of the room. Our arrangements with the hotel are just
24 to have those in the morning, but if you buy a cup at
25 the hostess desk at the coffee shop, I understand that

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1 you can refill that all day long at no charge if you
2 keep your cup, so for tomorrow and the rest of the days
3 you may well want to just refill with the hostess at the
4 coffee shop. All right, are there any questions for Dr.
5 Folwell about Exhibits 27, 28, and 29 that would be in
6 the nature of voir dire? There are none. Is there any
7 objection to the admission into evidence of Exhibits 27,
8 28, and 29? There are none. Exhibits 27, 28, and 29
9 are hereby admitted into evidence. Now if you have any
10 additional questions of Dr. Folwell about those exhibits
11 you may ask them at this time. Mr. Carswell?

12 MR. CARSWELL: I just have one. On Exhibit
13 27, near the end in the conclusions, do you say that on
14 the bottom of page 16, first column, you say the degree
15 of price variability during the life of the present
16 order has been less than half that experienced
17 otherwise. Does this take into account the drastic
18 price swings in the early '80s?

19 DR. FOLWELL: I previously attempted to answer
20 that question and I believe -- and I don't have a copy
21 of the student's thesis with me, but I believe the data
22 ran through -- I'm trying to find it here -- through
23 1979, so it wouldn't have had that sharp increase that
24 occurred in '80, '81, '82.

25 MR. CARSWELL: Thank you very much.

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1 ADMINISTRATIVE LAW JUDGE: Any other questions
2 of Dr. Folwell? Yes, Mr. Roy?

3 MR. ROY: Dr. Folwell, with your experience
4 with the last marketing order, did you experience or
5 hear of any complaints from any of the breweries around
6 the world for the lack of hops from the marketing order?
7 The last one?

8 DR. FOLWELL: No, not really. And I sat at
9 the table with -- well, you said from brewers?

10 MR. ROY: Yes, yes.

11 DR. FOLWELL: No, I did not.

12 MR. ROY: Okay. One last question. How --
13 could you explain how you came to be involved with this,
14 your presentation today?

15 DR. FOLWELL: Of course, sitting on the
16 previous marketing order was one factor that contributed
17 towards it. Another one was possibly the fact that we
18 had done this research on the previous marketing order,
19 which I will tell you made people in the administrative
20 committee nervous that we delving into their behavior
21 and looking at it to see whether they unduly restricted
22 the flow of hops. Another possible reason would be that
23 a number of the hop brewers have been students of mine
24 at the university over time and possibly the last one
25 was that a group of hop growers called me, I believe

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1 last spring, late last spring to indicate that they were
2 proposing this order and I had a meeting with them for
3 approximately an hour earlier this year. It must have
4 been in April, because I was going out to an asparagus
5 field, also.

6 MR. ROY: And since that time, your
7 involvement has been -- have you received any
8 compensation for your...

9 DR. FOLWELL: No. I even paid for my own
10 lunch today.

11 MR. ROY: Thank you, Dr. Folwell.

12 ADMINISTRATIVE LAW JUDGE: Is there any reason
13 why Dr. Folwell could not be excused at this time? He's
14 welcome to stay, but he wouldn't be required to. Mr.
15 Monahan, do you have anything else for him?

16 MR. MONAHAN: No, Your Honor.

17 ADMINISTRATIVE LAW JUDGE: All right. Dr.
18 Folwell, thank you so much.

19 DR. FOLWELL: Thank you.

20 ADMINISTRATIVE LAW JUDGE: You may step down.
21 Now, as I understand it, today is economists day. So
22 who would be the next one to testify?

23 MR. MOODY: It'll be Dr. Mark Jekanowski from
24 Sparks.

25 ADMINISTRATIVE LAW JUDGE: All right. Dr.

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1 Jekanowski, you may come forward.

2 UNKNOWN: Do you have a technical unit?

3 ADMINISTRATIVE LAW JUDGE: Yes, we'll be off
4 record for two minutes.

5 ***

6 [Off the Record]

7 [On the Record]

8 ***

9 ADMINISTRATIVE LAW JUDGE: We're back on
10 record at 2:59. Dr. Jekanowski, would you again state
11 your full name and spell it for the record?

12 DR. JEKANOWSKI: My name is Mark David
13 Jekanowski. M-a-r-k D-a-v-i-d J-e-k-a-n-o-w-s-k-i.

14 ADMINISTRATIVE LAW JUDGE: And before you
15 begin your testimony and your presentation, would you
16 just acquaint us with your educational background and
17 your work experience?

18 DR. JEKANOWSKI: Sure.

19 MR. MOODY: Excuse me, Your Honor? If it's
20 all right, can we have an oath first?

21 ADMINISTRATIVE LAW JUDGE: Oh, thank you, Mr.
22 Moody. The oath. Would you raise your right hand,
23 please?

24 ***

25 [Witness sworn]

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ADMINISTRATIVE LAW JUDGE: Thank you.

MS. DESKINS: Your Honor, I have one other thing. I know last time Mr. Moody had trouble looking at the overheads. Is there a copy that can be provided to him?

ADMINISTRATIVE LAW JUDGE: Mr. Jekanowski, you may now distribute copies of the presentation.

DR. JEKANOWSKI: Okay. I have one, two, three, four, five. They're a little bit -- well, let me give one to Mr. Moody to start. They're a little bit small print, but I think Jim is familiar with the presentation.

MS. DESKINS: Your Honor, maybe this would be another thing to bring up for the record. We seem to be having the continuing problem of people not bringing in enough copies. I think what's pretty apparent is you need to bring in, I would say at least 15, because the lack of copies is holding things up and time is becoming an issue, so maybe in the future we could remind everyone to bring a sufficient number of copies.

DR. JEKANOWSKI: Okay.

ADMINISTRATIVE LAW JUDGE: Thank you.

DR. JEKANOWSKI: And I apologize for that.

Actually, what happened was they were in the process of

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1 printing out 12 and the printer jammed and they lost the
2 original, so I just found out now that I don't have the
3 full amount of copies. But I do have...

4 ADMINISTRATIVE LAW JUDGE: Court reporter.
5 Mr. Carswell's willing to give up one of his. That's
6 good. Will you want this to be an exhibit that goes in
7 the official record, Dr. Jekanowski?

8 DR. JEKANOWSKI: Yes, I would.

9 ADMINISTRATIVE LAW JUDGE: All right. If you
10 also want the typist to have a copy for any terms you're
11 using that the typist may be unfamiliar with, then the
12 court reporter will need an additional one.

13 DR. JEKANOWSKI: I'll provide one.

14 ADMINISTRATIVE LAW JUDGE: All right. Now,
15 this should be marked, then, as Exhibit 30. I'm going
16 to ask the court reporter to mark that as Exhibit 30.
17 All right, you were going to tell us about your
18 education and your work experience.

19 DR. JEKANOWSKI: Okay. I hold a bachelor's
20 degree from University of Massachusetts in Amherst in
21 Resource Economics and a masters and Ph.D. degree in
22 Agricultural Economics from Perdue University. After
23 leaving Perdue, I worked with USDA's Economic Research
24 Service for about three and a half years prior to coming
25 to Sparks and I've been employed as an economist with

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1 Sparks for, I think, the past three years.

2 ADMINISTRATIVE LAW JUDGE: And would you
3 describe for us what type of company Sparks is and in
4 what part of it you work?

5 DR. JEKANOWSKI: Sure. Sparks is an economic
6 consulting company. It -- we believe we're the biggest
7 of our type of consulting company in agriculture. We
8 work primarily with agricultural firms doing market
9 analysis, helping to -- helping firms manage risks,
10 manage inventories. And we also do general consulting
11 such as benefit cost analyses and for firms interested
12 in entering different types of industries and whatnot,
13 and also policy analysis. And I work in the Washington,
14 D.C. office of Sparks and my responsibilities are
15 primarily focused on agriculture policy analysis.

16 ADMINISTRATIVE LAW JUDGE: Thank you. So
17 since your achieving your Ph.D., have you had about six
18 or seven years in working in economics?

19 DR. JEKANOWSKI: That's right, yeah. Five and
20 a half to six, I would say.

21 ADMINISTRATIVE LAW JUDGE: All right. Thank
22 you. You may proceed.

23 ***

24 MARK DAVID JEKANOWSKI,
25 having first been duly sworn, according to the law,

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1 testified as follows:

2 DR. JEKANOWSKI: Okay. As you see, I have a
3 presentation here and I again apologize for not having
4 as many handouts as I would like, but what I plan to do
5 is go through my presentation line by line and I'll sort
6 of paraphrase where possible, or where I think
7 appropriate, but I think the presentation really lays
8 out, from my perspective, the argument why this
9 marketing order is generally not a good idea, bad for
10 the industry. Aside from the fact that it will create
11 winners and losers within the industry, I also believe
12 it's just fundamentally not going to work and not going
13 to achieve its intended goals. And I should also note
14 that I'm -- I don't claim to be an expert in hops.
15 Prior to working on this project, I -- my only
16 experience with hops was through the end product. I
17 didn't know what a hop plant looked like, but what I am
18 is an economist, and what economists do is study markets
19 and study the effects of different constraints on
20 markets and really try to look at unintended
21 consequences of different policy shifts, or policy
22 changes, and that's really the capacity with which I
23 entered this project. And I think that, from my own
24 perspective, this marketing order provides a
25 fascinating, almost text book case of a policy that will

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1 provide tremendous unintended consequences and it
2 ultimately won't work and ultimately can't work. And I
3 hope to demonstrate why over the course of my
4 presentation. Just to kind of get us all on the same
5 page. I wanted to go briefly through the key provisions
6 of the marketing order. We heard a fair amount of
7 testimony from different proponents who testified that
8 there's a need for a marketing order, but then when
9 quizzed, they -- you know, said that they didn't
10 necessarily study this proposal, in particular. But I
11 think, in order to really get a handle and an
12 understanding of what the effects of this marketing
13 order are, or will be, we need to at least briefly go
14 through what the key provisions are and what -- and why
15 those provisions will ultimately affect the market.
16 First of all, as has come out throughout the testimony
17 in both direct and cross-examination deal -- the main
18 provision, or one of the main provisions of this
19 marketing order is allotments, producer allotments,
20 which will be issued based on each producer's highest
21 alpha production between 1997 and 2002. Highest alpha
22 acid production. And a committee, I believe, of eight
23 people it was proposed, will set a saleable quantity,
24 which will legally limit the amount of alpha acid
25 marketable each year by each grower. At least, that's

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1 my understanding from a non-legal perspective from
2 reading the provisions. It will also develop, or
3 establish a reserve pool. And we haven't heard any
4 testimony so far about how the reserve pool will operate
5 or what a reserve pool is, but I think it's sufficient
6 to say that the reserve pool will be the sole outlet for
7 hops produced in excess of the saleable. So any grower
8 who produces more hops than he is allowed to under the
9 saleable, can only send his hops to the reserve pool.
10 So that's what really restricts the supply to the
11 market. And those hops are held off the market until
12 the following year, or until approved by the committee.
13 Other provisions of the marketing order, severe
14 restriction on entry of new growers -- and I'll go
15 through in some of my later testimony to describe these
16 restrictions and their likely implications. And I think
17 it's also readily acknowledged that allotments can be
18 sold, leased, or traded among growers, although I'm not
19 real clear on whether they can be leased or not, but it
20 can at least be transferred, sold, among growers. So I
21 think that sort of should put us kind of all on the same
22 page so we kind of know the basic provisions of this
23 marketing order. Now, I think it's worthwhile to sort
24 of step back and take a sort of text book definition
25 kind of analysis of production controls generally, which

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1 I believe this marketing order, it is a form of
2 production control. And ultimately, the concept is to
3 restrict supply to affect prices and it's to raise
4 prices. And despite what we hear that the intention is
5 to provide orderly marketing and you know, not
6 necessarily raise prices, I think it's fair to say that
7 if prices were at historic highs right now, we wouldn't
8 be sitting here talking about a marketing order. I
9 mean, the goal here, whether it's implied or explicit,
10 is to raise prices by restricting supply, in my belief.
11 So again, back sort of to the text book, you know,
12 requirements for how this might be possible. I think
13 one of the obvious necessary conditions for it is strict
14 enforcement with strict penalties, so in this case, I
15 believe it's dealers who are regulated and restricted on
16 what they can purchase from growers and ultimately sell
17 to their consumers. And we heard a little bit of
18 testimony or cross-examination, at least, by Mr. Moody
19 about what some of those penalties would be under this
20 marketing order, if you get caught selling beyond your
21 saleable, or even not keeping the right types of
22 records, or et cetera. So there certainly has to be
23 penalties in place and they have to be severe in order
24 to make this concept work. But aside from that, there's
25 also a lot of conditions, a lot of market conditions

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1 that would be preferred in order for this type of policy
2 to achieve its stated goals. And those conditions
3 include border controls, in other words, some type of
4 restriction on what we can import. Again, I think it
5 came out over and over, maybe, you know, just constantly
6 in the cross-examination that if you only restrict 25
7 percent of the market, you have the remaining 75 percent
8 of the world market, potentially, as the source of
9 import. So ideally, we would have some kind of border
10 control, some quotas in place, or very stiff tariffs
11 that would restrict supplies coming in. Another
12 preferred condition is an inelastic demand and price
13 response and that was, in fact, given as one of the
14 justifications for this marketing order. But I think
15 from testimony this morning in cross-examination and
16 then, I think, just among economists, generally, there's
17 some disagreement on whether the hop market is
18 characterized by an inelastic demand and price response.
19 But nevertheless, that's a preferred condition. Another
20 preferred condition is perfect foresight by the central
21 planner. Again, this hop marketing committee is
22 speaking on behalf of the entire industry in determining
23 what every grower, essentially, can produce and -- well,
24 not produce -- I'll be careful there -- but,
25 essentially, it's determining what the entire industry

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1 can supply into the market. So it would certainly help
2 if we had a real precise, accurate measure of
3 forecasting what the future demand and supply will be.
4 Another preferred condition is -- would be simplicity
5 and accuracy in measuring output. Now, in this case
6 we're regulating -- or the -- the order proposes to
7 regulate alpha acid and just as I can't claim to be an
8 expert in hops, I'm also not a chemist, but I think it's
9 worth at least examining the accuracy with which alpha
10 acid can be measured and different types of hops and
11 under different conditions and whether, you know, the
12 degree to which this output can be accurately measured.
13 And another condition is -- would be, ideally, the
14 product that we're regulating is ultimately
15 indistinguishable. It's a commodity product and would
16 -- with little need for substitution within the
17 regulated market. And my, you know, key point in
18 thinking about these preferred conditions -- and I think
19 this came out and it's coming out over and over again in
20 the -- especially in the cross-examination, is that most
21 of these preferred conditions, if not all of them, are
22 absent in the current hop industry and the result of
23 that will be ultimately, could be order -- this
24 marketing order won't achieve its stated goals. So
25 again, just sort of continuing a sort of a text book

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1 case of supply controls, text book case of this
2 allotment program, it's worthwhile to think of the short
3 run and the long run. Market impacts, if you will. And
4 I think we could possibly say that in the short run, any
5 restriction on supply might artificially boost prices.
6 Might raise prices above current levels. It's just a
7 common, you know, characteristic of the supply curve. A
8 common knowledge of economics would tell you that if you
9 restrict supply, you might boost prices al el sequel
10 [ph]. But the al el sequel caveat there sort of becomes
11 less binding pretty quickly and then we can look at the
12 long run. Once markets adjust, what happens after the
13 supply is restricted. And I think it's safe to say I
14 don't think that any of these conditions would be in
15 dispute among economists that in the long run, any
16 revenue gains associated with increased prices that are
17 affected by this marketing order will get capitalized
18 into the allotment base. And I'll talk more about that
19 later in my presentation. Also, I think it's safe to
20 say that the customers -- in this case, the brewers or
21 the dealer -- will search for alternative sources of
22 supply, alternative sources of hops, and that means in
23 most likely foreign supply, maybe even supplying
24 different states in the US. We just don't know.

25 ADMINISTRATIVE LAW JUDGE: Let's change the
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1 tape.

2 ***

3 [Off the Record]

4 [On the Record]

5 ***

6 ADMINISTRATIVE LAW JUDGE: All right, we
7 changed the tape at 3:17. It's still 3:17. You may
8 continue, Dr. Jekanowski.

9 DR. JEKANOWSKI: Okay. Thank you, Your Honor.
10 Just continuing on here. Looking at the long run
11 effects of these types of supply controls. I think it's
12 safe to say that any higher market prices, world market
13 prices that would result from this marketing order would
14 also encourage investment in new planting in other
15 growing regions that aren't regulated -- overseas,
16 particularly. I think it's also safe to say that
17 domestic incentives for technological innovation are
18 reduced. I think you should -- we need to sort of ask
19 ourselves that whether -- for instance, whether high
20 alpha hops ever would've been developed if the marketing
21 order were in place. And I think Mr. Carswell pointed
22 this out. In most cases, economists think technological
23 change is a good thing. If you can more of a product on
24 less resources and less land, that's -- society benefits
25 from that. But by regulating alpha acid, for instance,

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1 in this manner, I think incentives to increase
2 productivity further, are clearly, clearly sacrificed.
3 And ultimately, US competitiveness is sacrificed. The
4 benefits primarily go to other producers, to foreign
5 producers who can supply the market at the expense of
6 the US industry. Now, kind of getting away a little bit
7 from the text book theory, I think it's worthwhile to
8 kind of step back and take a look at some of the basic
9 characteristics of the hop industry today, at least my
10 understanding of the hop industry. I think it's safe to
11 say that everybody in this room would agree that the hop
12 market is global and that prices are determined in the
13 world markets. And we believe that the US share of
14 world production is roughly 25 percent. Maybe we don't
15 know exactly what it is, but we certainly know it's far
16 less than 50 percent and maybe more than 10 percent, so
17 we're kind of using 25 percent as a benchmark. I think
18 it's also safe to say that if there's any border
19 controls that are currently in effect are very minor.
20 There's a minor duty for leaf hops and a minor duty for
21 extract. And by minor, I mean minor in terms of in
22 relation to the value of that product that's bough and
23 sold in markets. So they're certainly too low to cause
24 any severe restriction on imports. We also know -- or
25 at least the data shows -- the value of US hop exports

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1 are trending higher and that the trade surplus is
2 growing. Ultimately, we're exporting the value of our
3 exports is greater than the value of our imports of
4 hops. And finally -- and I think this came out pretty
5 clearly in this morning's testimony that the degree of
6 price elasticity is very much open to debate in the hop
7 industry. It's certainly true -- I'll buy the statement
8 that there's few substitutes for alpha acid, but looking
9 at the market on a global scale, you know, the US market
10 is open to foreign trade, which would imply a more
11 elastic price response. Now, just -- I mentioned on my
12 earlier slide here that US balance of trade is
13 increasing. This is just data right from the Hop
14 Growers of America, from the statistical packet that
15 they put out each year, and I think it's interesting to
16 note that -- I marked out the period during -- at least,
17 for the time period that I had for the data going back,
18 I marked out the period before -- or I should say during
19 the previous marketing order and after the current [sic]
20 marketing order. And you know, a few things are evident
21 here and you know, the -- you know, correlation isn't --
22 doesn't necessarily imply causality, but I think it's
23 safe to say that after the demise of the last marketing
24 order and after those supply controls were lifted, our
25 trade balances increased, which to me implies that the

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1 competitiveness of the US hop industry has increased
2 over time. It trended higher. Certainly, its variable
3 on the trend is certainly up. Now, you might want to
4 point out that big jump in the year 1979 to 1980, but
5 it's my understanding that that is the time period that
6 corresponds with the major German crop failure, so it's
7 not surprising that we had to export, at that period, to
8 supply the market. But if you get rid of that one data
9 point there, I think it's pretty clear that exports --
10 the balance of trade was, at best, steady or trending
11 lower. Now, back to some sort of text book analysis of
12 what we can expect from these types of supply controls
13 are from this market order, in particular. Again, I'll
14 just go through these quick, because we've sort of hit
15 on them over and over again, but I think it's clear to
16 say that any restriction on US supply will provide
17 signals for foreign competitors to increase their own
18 supply. I mean, you can ask yourself if you knew that
19 Germany was going to decrease their supply by some
20 percent, I think most hop growers in this room would
21 probably take that as a signal to increase their own
22 production and I don't think there's any reason to think
23 that German producers or Chinese producers or maybe
24 French producers aren't going to ultimately react in the
25 same way. Again, product flows freely across national

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1 borders. I think I mentioned that already. And again,
2 even just the expectations of reduced US supply provide
3 a signal to competitors to increase. If I were a German
4 producer right now and I saw the US hop industry
5 seriously considering instituting a market order, I
6 think I'd start, you know, ramping up my readiness to
7 plant more hops. It's just a signal of what's to come,
8 especially if the intent is to raise world market
9 prices. Another point, sort of text book results,
10 supply controls stifle -- supply controls of this type
11 stifle domestic innovation and technology adoption. I
12 think I mentioned that one already. Certainly decreases
13 the incentives to reduce costs and improve efficiency
14 and it also decreases incentives to explore new markets
15 and product uses. It really takes the burden off the
16 growers or off the industry, of finding ways to grow the
17 industry. If all you're thinking about is how to
18 restrict the industry to raise prices, it clearly
19 provides less incentives to try to grow the industry.
20 And it also, as I'll show later in my testimony, has a
21 potential to increase costs, which is also, you know,
22 adding -- potentially adding to inefficiency in crowding
23 out investment in new technology. But I'll cover that a
24 little later in my testimony, as well. A couple of more
25 unintended consequences and some of these are actually

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1 intended, you know, it restricts individual producers'
2 ability to respond to market signals. I think that's
3 the intent of this marketing order, basically, that some
4 producers don't want other producers to keep production
5 at their current level, or some producers don't want
6 other producers to increase their production. So
7 certainly, that sort of erodes the ability for
8 individual producers to make their own choices and to
9 respond to market signals as they see them. It imposes
10 burdensome costs on producers hoping to expand, increase
11 efficiency, or take risks. I think clearly, again, this
12 came out over and over in the cross-examination. If
13 supply restrictions increase the value of base, that's a
14 burdensome cost on some producers. I don't think
15 there's any way around it. And again, it inevitably
16 will lead to a market for allotments and inequitable and
17 inefficient transfers of wealth among producers. And
18 I'll address that point in more detail real soon. Okay,
19 this is just -- this slide just kind of gives a brief
20 review of the issues I'm going to cover in the upcoming
21 slides. Sort of keeping the focus on economics and
22 economic theory, I want to first review the inequity of
23 base allocation under this proposed marketing order. I
24 want to talk a little bit about setting the saleable
25 quantity. I guess I agree with Dr. Folwell that we

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1 don't know what -- we don't know exactly what the
2 saleable quantity will be, but I think we can come
3 pretty close. We can -- based on some assumptions that
4 we can make, we can come up with a pretty good idea of
5 where we might end up in the first year. I want to talk
6 a little bit about markets for allotments, inter-
7 industry wealth transfers, distribution of costs and
8 benefits -- that's basically the same as inequity or
9 base allocation -- potential negative effect on aroma
10 hops. Even though the proponents of the marketing order
11 seem to admit from time to time that the problem isn't
12 in aroma hops, it's in alpha production, but I don't
13 think there's any way to get around the fact that this
14 marketing order will affect aroma hops and have a
15 negative effect. And I also want to talk a little bit
16 about implications for the entry of new growers.

17 ADMINISTRATIVE LAW JUDGE: Beginning now, Dr.
18 Jekanowski, would you state the page number of your
19 slide as you go on to the next one?

20 DR. JEKANOWSKI: Sure. Okay, moving to slide
21 10 on page four of my handout -- okay, yeah. I'm going
22 to go through these real quick. I actually -- I did
23 this at the beginning of my presentation. Marketing
24 order specifics. And this -- these are what I'm going
25 to use to do my little analysis of the effects on

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1 transfers of wealth and setting the allotment. Okay, we
2 know that the base allotments will be allocated
3 according to the highest alpha production from 1997 to
4 2002. We also know that the alpha base determination
5 considers the actual alpha for varieties over 10
6 percent, while lower yielding varieties are provided a
7 flat 10 percent. I don't think -- that's straight out
8 of the proposed language. And we also know that most
9 recent year production is ignored. And I presume that
10 will always be the case, even if this marketing order
11 didn't come into effect next year, but maybe the year
12 following, perhaps they'll update the years, but in any
13 case, the most recent year production is always ignored.
14 Okay, moving to slide 11, again on page four of my
15 handout. So what I'd like to do now is do sort of a
16 rough analysis and I'll admit, this is a back-of-the-
17 envelope type of analysis, but I think it's pretty
18 powerful, nonetheless and I'd like to determine the
19 likely scenario for industry-wide base allotment in
20 saleable quantity. In one -- my finding -- or, you
21 know, one of my main findings -- will depend upon the
22 fact that industry allotment, as designed, will far
23 exceed recent alpha production trends. In other words,
24 in the way economists would refer to this is that the
25 initial base will not represent a competitive

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1 equilibrium in this industry. And I find it interesting
2 that actually, in testimony in Portland, I got the
3 impression that perhaps the proponents thought that this
4 was a benefit. That having excess base available was a
5 positive aspect of their proposal. I think it's just
6 the opposite. I think this excess base available is
7 what will exacerbate the need for wealth transfers among
8 producers and ultimately lead to price -- for
9 allotments. And I'll follow through my reasoning here
10 in a second. But be that as it may, if you have a
11 dramatic inflated base, an inflated allotment base, it
12 will, by design, require a dramatic cut in the saleable
13 in order to reduce supply. And again, the degree of
14 wealth redistribution will be amplified by this inflated
15 base. Now how do I come up with these conclusions? On
16 slide 12 of -- again, of page four of my handout, just
17 based on the industry characteristics that we know from
18 the statistics that are provided to us, we know that hop
19 production is trending lower and it has certainly
20 trended lower between 1997 and 2002. We know that aroma
21 acreage accounts for between 30 and 40 percent of the
22 total supply. We know -- or at least, I know now -- I
23 now know from the people in the hop industry who have
24 been -- who have taught me about this, that alpha acid
25 from aroma hops averages about six percent or less,

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1 sometimes far less, but just based on the language of
2 the order, the allotment will assign a flat 10 percent.
3 And I think it shouldn't be in dispute that given these
4 characteristics, all growers will choose their highest
5 alpha production during this 1997 to 2002 period, also
6 taking into account the hop -- the aroma hop premium.
7 So just to sort of give a little visual of hop
8 production, again, this is straight out of USDA/NASS
9 data. This isn't alpha acid, this hop pounds, but just
10 -- I mean, it does illustrate clearly hop production is
11 trending lower, or has been trending lower since 1997.

12 ADMINISTRATIVE LAW JUDGE: Would you tell us
13 about the acronym NASS? What...

14 DR. JEKANOWSKI: Oh, I'm...

15 ADMINISTRATIVE LAW JUDGE: ...letters are
16 included and what it means?

17 DR. JEKANOWSKI: Yeah, NASS is USDA's National
18 Agricultural Statistics Service. It's sort of the main
19 market reporting service of USDA. Again, just to recap
20 here, because I don't want anybody to lose this fact
21 that aroma hops contribute a flat 10 percent for base.
22 And then I did make a few assumptions in my analysis.
23 And they're assumptions that are actually sort of based
24 on actual industry statistics as best as I could collect
25 and these assumptions include the bitter hops, in other

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1 words, alpha hops, have been increasing in their average
2 alpha percentage over time and just based on a weighted
3 average of production by variety over this time period,
4 and using the alpha percentages that are on the Hop
5 Growers of America's web page, I estimated that the
6 alpha composition of alpha hops was about 12 and a half
7 percent in 1997 and it increased to 13 percent in 2002.
8 And I think that that's very conservative, especially
9 knowing that there's some super-high alpha varieties out
10 there that far exceed these numbers. Of one assumption
11 is that all growers will know their past production
12 trends and alpha averages without any cheating.
13 Clearly, there'll be incentives to cheat, but we'll
14 ignore that for a moment. And again, just to recap, all
15 growers will demand their base equal to the highest
16 estimated alpha production. Okay, moving to slide 15,
17 just based simply on those industry facts, we can come
18 up with a rough estimate of the lower bound for an
19 industry base. And that's simply based on the fact that
20 1997 was the highest year for alpha production -- again,
21 taking into account the fact that all aroma hops
22 produced that year will contribute 10 percent, much
23 higher than alpha. So if we assumed that there was only
24 one grower in the industry, if the industry was
25 represented by one grower, he or she would certainly

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1 pick 1997 to set his or her base. So again, that gives
2 us a lower bound, but it's at a very conservative lower
3 bound because certainly, some producers increased over
4 this time and will pick 2002 or 2001 instead of 1997.
5 But again, this gives us a very conservative starting
6 place. Moving on to slide 16, this lower bound that I
7 calculated based on my simple analysis comes up to about
8 8.7 million pounds of alpha based on what the alpha
9 production was in 1997 and based on this aroma market
10 premium. So it exceeds 8.7 million pounds. Now, I
11 don't think, given that some producers will choose years
12 later than 1997 because their production has increased,
13 I don't think it's unreasonable to inflate that
14 slightly. And I inflate it just a little bit, five
15 percent to account for the fact that some producers will
16 choose a later year and so from that I come up with a
17 very conservative base estimate of about 9.2 million
18 pounds of base. Now, to put that into perspective, the
19 actual alpha production in 2002 was about 6.9 million
20 pounds and the average production from 1997 through
21 2002, over this whole period, was about 7 million
22 pounds. So clearly, the base is starting out highly
23 inflated. Based on that, without even considering an
24 effect on supply, the saleable quantity will have to be
25 set at roughly 75 percent just to equal 2002 production.

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1 So that's not even talking about a cut in supplies.
2 Basically, we're starting out from 75 percent. Okay,
3 moving on to slide 17. Again, 2002 alpha production was
4 6.9 million pounds. Again, to sort of continue this
5 back-of-the-envelope analysis, let's assume that
6 objective of the committee was to reduce stocks that are
7 -- reduce the amount of stocks in the market and we've
8 heard, you know, references to the fact that there's
9 excess supply in the market and maybe stocks are too
10 high. So let's assume that we want to decrease stocks
11 to 2001 levels. Now, again, USDA -- the National Ag
12 Statistic Service estimates that as of September 1 of
13 this year, stocks held by dealer growers -- now, this is
14 assuming the category that we want to decrease -- stocks
15 held by dealer growers were about 34 million pounds.
16 Now, just merely for simplicity, because it makes the
17 math easy, let's assume that they average 10 percent
18 alpha. That implies that stocks held by dealer growers
19 in -- as of just a couple of months ago were about 3.4
20 million pounds of alpha. Now, if we assume a perfectly
21 stable market with no changes in the demand or exports
22 or imports or domestic use characteristics, to draw down
23 stocks to 2001 levels, when they were -- when USDA
24 reports that were 16 million pounds, that would require,
25 again, assuming at 10 percent alpha, that would require

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1 a 1.8 million pound decrease in alpha production for
2 next year. So moving on to slide 18, again, just to --
3 I want to keep in your mind the fact that 2002 alpha
4 production was 6.9 million pounds -- and reducing alpha
5 stocks to 2001 levels requires 1.8 million pound
6 production decrease next year. That implies that next
7 year the committee would -- could conceivably set the
8 saleable at 5.1 million pounds of alpha. Again, with
9 the inflated base of 9.2 million pounds, that comes out
10 to a saleable of 55.4 percent. And again, I think that
11 -- you know, you can do your own back-of-the-envelope
12 analysis. I think I was conservative in every turn
13 here. Conservative in terms of what the actual base
14 will be. Probably conservative in terms of what the
15 saleable will be. And still, we come up with a saleable
16 of 55 percent. Again, recalling that we're starting out
17 at 75 percent just to even not affect supply. So what
18 does that mean? Moving on to slide 19. If nothing
19 else, I think the most -- for lack of a better word --
20 offensive aspect of this marketing order is the
21 transfers of wealth between producers that will result
22 from this very characteristic of the marketing order.
23 And I'm going to do a couple hypotheticals here. I know
24 that we like hypotheticals. But again, you're free to
25 question my assumptions. I think they're pretty sound.

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1 But let's consider two farms. Farm number one has
2 declining acreage over time and has generally not
3 invested in new technology, has generally -- new
4 varieties or improved varieties. They grow a hundred
5 percent cluster, which -- with an average alpha of eight
6 percent and a yield of 1870 pounds per acre. And these
7 -- I'm not really making those numbers up, I -- those
8 are based on, you know, the range of yields and alpha
9 percentages that provided right on the Hop Growers of
10 America's web page. Okay. So that's farm one, clearly
11 declining over time. Now, farm two is in a little bit
12 different situation. Let's assume that his acreage has
13 been increasing over time and in 1997, he was identical
14 to farm number one in that he was growing 100 percent
15 cluster variety and then -- but after 1997 he started
16 investing in high alpha hops, perhaps because he had
17 contracts for his alpha production. And as a result,
18 his average alpha increased from eight percent in 1997
19 to let's say 15 percent in 2002 and at the same time
20 yields also increased from 1870 pounds per acre, again,
21 the same as farm number one to 2400 pounds per acre in
22 2002. And this just putting the numbers up. I just
23 kind of assumed the direct trend, I mean, there's
24 nothing fancy here, but it's showing that the alpha
25 production in the yield and acreage for these two

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1 separate -- for these two hypothetical farms. You
2 might, you know, think about your own production in this
3 example, instead, if you don't want to use the
4 hypothetical. But now, let's return to the fact that we
5 think that the saleable will be set at 55 percent or
6 less. So what's the implication there? Well, for one
7 thing, considering farm two, this guy who's been
8 expanding because maybe he has a, you know, the market
9 opportunities to market his hops. Again, 2002
10 production, or -- yeah. No -- excuse me, 2003
11 production is ignored and it actually equals 353,000
12 pounds of -- 353,600 pounds of alpha. That's the bar on
13 the far -- it would be your right. Now, he's going to
14 choose his base based on his highest historic
15 production, so clearly, he's going to be limited to
16 2002, whatever he produced in 2002, which in this case
17 was 300,000 pounds. So that's where he's starting out.
18 Now, if we set the saleable at 55 percent of that, then
19 that allows him to market freely 165,000 pounds of hops,
20 which is actually only 47 percent of what he marketed in
21 2003. So again, the additional base that he'll need to
22 purchase to maintain trend production is roughly 235,000
23 pounds and just to equal 2003 production, in other
24 words, to not even increase his supply, he'll need to
25 acquire about 188,000 pounds of base. So that's farm

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1 two. Well, now let's take a look at farm one under the
2 same condition of a 55 percent saleable. Now, he's
3 going to choose base equal to his highest production,
4 which is going to be 1997. Now, you might be wondering
5 well, how come his base comes up to 187,000 pounds,
6 which is clearly higher than his 1997 production. But
7 the reason is that his hops produced less than 10
8 percent alpha, so he's given an automatic boost right
9 from the start. And now he set his saleable at 55
10 percent, everybody's subject to the same saleable. That
11 implies 102,000 pounds of alpha he can market which,
12 again, 2003 isn't considered by the marketing order. So
13 despite the fact that he's facing a 55 percent saleable,
14 he still receives excess allotment for use or sale of
15 20,750 pounds, excess beyond what he produced in his
16 most recent year. So clearly, he will be able to higher
17 increase his production despite the marketing order, or
18 sell his base to somebody who might need it more. I
19 don't think this point can be overstated. Moving on to
20 slide 23. Again, the industry base will far exceed
21 normal production. A conservative saleable estimate
22 could be 55 percent or less. And on these two
23 hypothetical farms that I discussed, the expanding
24 producer will need to purchase 53 percent more alpha
25 base just to maintain his 2003 production for really an

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1 effective saleable of 47 percent facing that producer.
2 While the declining producer will be rewarded with 25
3 percent more alpha base than he or she produced in 2003.
4 So that grower's effective saleable is 125 percent. So
5 maybe -- in our testimony and in some of the testimony
6 in Portland, some people were curious why, in cross-
7 examination, we would ask producers whether their
8 production increased or decreased over time. But I
9 think -- I hope that this example makes it clear the
10 inequity of the transfer of wealth or maybe their
11 business transaction between the declining producer and
12 the expanding producer. I think it's pretty clear.
13 There was some talk -- moving on to slide 24. There was
14 some mention that, you know, maybe the inflated base
15 will allow base to not take on a value, or at least not
16 to take on a very high value. But I don't think that
17 makes sense, economically, because base will be viewed
18 as a productive asset. It almost be definition has to
19 have a market value to those who need it, to those who
20 are faced with that constraint, they're going to have to
21 pay for it in order to gain access to it. Generally
22 speaking, this again is back to text book economics
23 here. Economics says that the unit price of base will
24 equal the present discounted value of all future
25 revenues from that base. So basically, the value of

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1 that base will be bid up to what somebody sees is all of
2 the future value to holding to that base. That's -- we
3 can't say exactly what the price of base will be from
4 the get-go, but we certainly know what will -- from
5 where the base will derive its value. And its supply --
6 it would depend on many factors. The supply of base --
7 tighter restrictions will increase its price and really
8 here the tighter restrictions would mean lower
9 saleables, especially, will increase its price. And the
10 expected future price of hops -- if growers think this
11 marketing order will increase the price, then they'll be
12 willing to pay more for it. And interest rates, to some
13 degree, because I assume that most growers will have to
14 borrow money to pay for their base. Moving on to slide
15 25. Just historically -- when I was -- when I started
16 doing this analysis, it became pretty clear to me that
17 there were more records out there of what base used to
18 sell for. Very few records are available. These
19 transactions occur in private, but estimates range from
20 about .20 per pound in the 1960s to well over a dollar a
21 pound in the early 1980s and even today we found out
22 that perhaps high as \$2 and I think in Oregon, in
23 Portland, one producer mentioned he paid 3.25. But in
24 any case, the price fluctuated wildly and was not a
25 minor amount. So to just kind of put this in

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1 perspective, assuming 10 percent alpha just because the
2 math is easy if we assume 10 percent, and again, that's
3 going to be conservative. If we -- if the price of base
4 averaged .50 over the life of the last marketing order,
5 then that would imply about \$5 for one pound of alpha
6 base under a similar situation. So again, to put that
7 in perspective, that expanding producer that I spoke of
8 just a few minutes ago, if he's required to purchase
9 188,000 pounds of base, that could cost him more than
10 \$900,000. And again, I can't overemphasize that all of
11 the estimates are conservative. I'm not hiding anything
12 here. I think I stated my assumptions very clearly. So
13 that producer who has a market for his hops and has
14 expanded because of he has a market for his hops could
15 be faced with next year having to incur almost a million
16 dollars in new, unexpected costs. If leasing is
17 available and that is an available option -- and that's
18 not clear to me, really, by the way the proposal's
19 written -- if leasing is an option, it would certainly
20 be a lower cost option for producers, but it would still
21 be a huge, burdensome, and unexpected new cost to that
22 producer. Moving on to slide 26, and to sort of address
23 this question directly, because it was sort of alluded
24 to in Portland, or at least I thought it was, that won't
25 the inflated base decrease the price of base, perhaps,

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1 to zero? Maybe if we have extra base out there, it'll
2 be freely available. That's increasing the supply,
3 it'll decrease the price. I mean, that's kind of the
4 logic that we were offered. But I think the answer is
5 absolutely not. That that's not the right way of
6 looking at this market. It's the saleable, not the
7 initial allotment that will determine how scarce base is
8 and ultimately will determine the price of base in the
9 market. The willingness to pay, in other words, the
10 demand for base, will reflect the degree to which some
11 producers are constrained by the allotment.

12 MR. CARSWELL: If you think you're on slide
13 26, you're actually on slide 25. Just so you know.

14 DR. JEKANOWSKI: Oh, you're right. My numbers
15 are slightly different. I'm sorry about that. Okay,
16 you're right. I am on slide 25.

17 MR. CARSWELL: I wanted to make sure you're on
18 the slide you wanted to be on.

19 DR. JEKANOWSKI: Yeah.

20 MR. CARSWELL: Sorry about that.

21 DR. JEKANOWSKI: Yeah, I am on the slide I
22 want to be on, but yeah, thank you for pointing it out.
23 Okay, slide 25. Again, the willingness to pay -- in
24 other words, the demand for base will reflect the degree
25 to which some producers are constrained by the

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1 allotment. So that farm two will be forced to have to
2 pay a large amount just to get the allotment that he
3 needs. And then I would also say that the degree of
4 wealth redistribution increases as base is inflated. So
5 this inflated base adds to the problem, it doesn't solve
6 the problem. It actually adds to the problem because
7 even without a cut in alpha supply under this scenario,
8 the expanding producers would have to buy base from a
9 declining producer. So again, if we assume that this
10 marketing order will work by restricting supply, will
11 work by raising prices by restricting supply, well, if
12 we set the saleable at 75 percent, that'll have no
13 impact on price, no impact on total marketings, but
14 it'll still require some producers to purchase base from
15 others. And I just point that out, again, these
16 hypotheticals. Same two farms -- oops. Oh, I'm sorry.
17 Actually, I didn't click it. You're absolutely right.
18 Let me just back up for a second and I'm looking at my
19 notes, but I should've been looking at the screen.
20 Again, to address the question of whether the inflated
21 base will decrease the price of base, perhaps to zero, I
22 think the answer is absolutely not. Again, recap. The
23 saleable is what determines the scarcity of base, not
24 the initial allotment. The willingness to pay for base
25 will reflect the degree to which some producers are

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1 constrained by the allotment and the degree of wealth
2 redistribution increases as base is inflated. And even
3 without a cut in the alpha supply, expanding producers
4 would have to buy base from declining producers. So now
5 I think I've caught back up on my slides and I'm going
6 to move to slide 27, which again, we're going to revisit
7 these two hypothetical farms. And just assume for a
8 minute that we set the initial saleable at 80 percent,
9 which again, based on my analysis, my back-of-the-
10 envelope analysis, would actually imply increase in
11 supply, not a decrease. It's actually implying an
12 increase in market supply. Well, the declining
13 producer, under this scenario, again with the same
14 187,000 pounds of initial base, would then have 52,350
15 pounds of base available to sell. Moving on to slide
16 28. The expanding producer or I should say the producer
17 who expanded over time, would be required to purchase
18 160,000 pounds of base just to maintain his trend or
19 113,000 pounds of base to equal his 2003 production. So
20 again -- and this is without a restriction on total
21 market supply. It's clearly a transfer of wealth within
22 the industry. So again, to recap real carefully here
23 what the implications are of the inflated base. And now
24 I'm on page [sic] 29. 80 percent saleable implies 7.4
25 million pounds of alpha, which far exceeds 2002

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1 production, so now it would appear to me not to be a
2 supplier restriction. But despite that, farm two must
3 purchase 113,600 pounds of base just to equal his 2003
4 production, which by the way, wasn't even considered in
5 his initial allotment base. And farm one, on the other
6 hand, has decreased over time, has 52,350 pounds
7 available to sell. So even without a restriction on
8 alpha supply, hence, no price impact, some farmers will
9 see sharply higher costs and those farmers who will
10 sharply higher costs are precisely the ones who
11 increased their production over time. Or who produce
12 high alpha varieties, perhaps. Okay, slide 30.

13 Implications for markets for base, which I think has
14 been acknowledged that there will be markets for base
15 and that base will have value. I don't think there's
16 any easy way to get around from the -- get around the
17 fact that it will be a new cost of operation for some
18 producers. And it will upset previous financial plans.
19 Another implication is that growers who are required to
20 purchase base simply to honor existing contracts could
21 get squeezed. If you recall, perhaps that expanding
22 grower expanded because he has contracts for his
23 production and he's, you know, legally obligated to
24 fulfill those contracts. But under this scenario, he'll
25 still be forced to buy base in order to honor those

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1 obligations. Again, if prices do not increase from the
2 hop marketing order -- HMO I'm using to refer to the hop
3 marketing order -- higher costs will -- I would say it's
4 safe to say higher costs will almost certainly force
5 some producers out of business. Again, going back to
6 this example. \$900,000, maybe a million dollars, just
7 to maintain your last year's production without a
8 restriction in supply. I think that could be pretty
9 hard for a lot of producers to swallow. And precisely
10 the ones -- precisely the producers who will be most
11 affected by that are what, I think as an economist, I
12 would consider the most efficient ones. Those who have
13 increased production over time and those who have
14 perhaps invested in higher yielding varieties.

15 MR. BARTON: May I take a break a moment?

16 ***

17 [Off the Record]

18 [On the Record]

19 ***

20 ADMINISTRATIVE LAW JUDGE: All right, we're
21 back on record at 4:14. Mr. Moody, before I recognize
22 you, I'd like to recognize Ms. Deskins.

23 MS. DESKINS: Thank you, Judge. I have two
24 procedural things and I want to get them in before the
25 end of the day is one of the rules of practice that

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1 govern these proceedings, anyone who gives an appearance
2 is supposed to say who they're representing and give the
3 name and address of them and I just want to clarify it
4 for the record, is Mr. Moody representing Sparks
5 Corporation or what's the representation here of any?

6 ADMINISTRATIVE LAW JUDGE: All right, Mr.
7 Moody, do you represent Sparks?

8 MR. MOODY: Sparks is the consultant, one of
9 our consultants for the hop opposition group. So in
10 that sense, yes.

11 MS. DESKINS: All right. And to also clarify,
12 is the hops opposition group, is that an association?
13 What is the nature of that group and if they have an
14 address, what is the address?

15 MR. MOODY: You're free to use my address is
16 its address, but it's unincorporated association of
17 opponents freely increased by any number of new members
18 as we go along through these hearings.

19 MS. DESKINS: Doesn't it have a board of
20 directors?

21 MR. MOODY: Well, I don't know if those are
22 appropriate questions, frankly.

23 ADMINISTRATIVE LAW JUDGE: Mr. Moody, I'm not
24 picking the sound up real well on your mike. It was
25 good before and it's not as good now. You may not be

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1 using the amplification mike, are you?

2 MR. MOODY: Yes. Yes, Your Honor.

3 ADMINISTRATIVE LAW JUDGE: Okay.

4 MR. MOODY: Although I think I agree. It's
5 not quite as loud as it was.

6 ADMINISTRATIVE LAW JUDGE: All right. Go
7 ahead, then. You know -- you don't think...

8 MR. MOODY: I was just saying I don't know
9 that, you know, I've always been concerned generally
10 representing opponents in these kind of proceedings,
11 that under cases like NAACP v. Blutton [ph] and things
12 like that, since there is the potential for everything
13 from selected enforcement to a selected handing out of
14 allotments and assigning percentages and whatnot, that
15 it -- other than opponents who choose to identify
16 themselves through testimony, I don't really think it's
17 a good idea that everybody who may privately choose to
18 vote no on this marketing order, should it go to
19 referendum, needs to have their name identified on the
20 record.

21 ADMINISTRATIVE LAW JUDGE: But the question
22 Ms. Deskins' asked you was not to identify everyone
23 who's a member of your association, but merely to ask if
24 there's a board of directors and that is an appropriate
25 question.

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1 MR. MOODY: Yes.

2 ADMINISTRATIVE LAW JUDGE: All right. Ms.
3 Deskins?

4 MS. DESKINS: Well, I'm just trying to get a
5 general idea, because the rules do require a name and an
6 address. I don't know that I need the street address,
7 but the city where they're located, just so we have some
8 idea of who this is for the record. And Mr. Moody, this
9 is -- these rules of practice have been around for a
10 long time. This has been true of any rule-making
11 proceeding.

12 MR. MOODY: No, I understand that and you're
13 right. Certainly, as you know, I have been doing --
14 you're free to ask growers who testify what their
15 address is and you're free to use my address as the
16 address for the association.

17 ADMINISTRATIVE LAW JUDGE: Mr. Moody, you have
18 a client who's a group, or a client that is a group, to
19 be correct grammatically. Your address we can certainly
20 have you put on the record and would you do that now?

21 MR. MOODY: Yes, Your Honor. It's 1101 30th
22 Street, Northwest, Suite 300, Washington, D.C., 20007.

23 ADMINISTRATIVE LAW JUDGE: All right. And
24 what is the name of your firm?

25 MR. MOODY: Advocates for a Competitive
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1 Economy.

2 ADMINISTRATIVE LAW JUDGE: All right. And
3 would you prefer that as you have representative members
4 of the group testify, that they give their address
5 individual -- as individuals, individual growers?

6 MR. MOODY: That's fine, Your Honor.

7 ADMINISTRATIVE LAW JUDGE: All right. And do
8 you have any name of the group that is your client other
9 than Hops Opposition Group?

10 MR. MOODY: Well, I always sort of like sexy
11 names like Front for the Liberation of Hops or something
12 like that. I think we'll just stick with what we've
13 got.

14 ADMINISTRATIVE LAW JUDGE: All right, so the
15 official address, then, for the Hops Opposition Group is
16 care of James Moody at Advocates for a Competitive
17 Economy and then the street address you gave?

18 MR. MOODY: Yes, Your Honor.

19 ADMINISTRATIVE LAW JUDGE: All right. Ms.
20 Deskins, do you believe that's adequate?

21 MS. DESKINS: Well, Your Honor, if Mr. Moody
22 won't provide any more, I'm unsure of what else we can
23 do. I mean, the rules do have a certain procedure that
24 they want followed.

25 ADMINISTRATIVE LAW JUDGE: All right. I sense
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1 that the composition of Mr. Moody's client is changing
2 as we go through this. Is that correct, Mr. Moody?

3 MR. MOODY: It's growing, Your Honor.

4 ADMINISTRATIVE LAW JUDGE: All right. I have
5 no objection to the group using counsel's address as
6 their address at this point. Now, I am concerned as to
7 the source of payment to Sparks for Dr. Jekanowski's
8 work. I think that should be identified, but we can
9 handle that when he's through with his direct testimony.

10 MR. MOODY: This might be a good time to bring
11 that up, Your Honor. He's got approximately an hour of
12 further direct and I'm wondering if we could a little
13 later tonight in an effort, at least, to finish up the
14 lion's share of the cross-examination, especially since
15 Dr. Folwell will be here only today.

16 ADMINISTRATIVE LAW JUDGE: You think by a
17 little later, we could finish cross? Uh-uh.

18 MR. MOODY: Well, at least a significant part
19 of it. You know, I'm concerned that at least Dr.
20 Folwell will have a chance to ask any questions he may
21 have.

22 ADMINISTRATIVE LAW JUDGE: All right. Since
23 Dr. Folwell will only be here today, I would like that,
24 as well, but I wouldn't imagine we could finish cross-
25 examination of Dr. Jekanowski tonight and I'd like to

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1 ask what his availability is on the other days that we
2 have scheduled this week and also Dr. Tweeten's
3 availability on those days. Dr. Jekanowski, would you
4 tell me which of the days this week you will continue to
5 be here?

6 DR. JEKANOWSKI: I plan to be here at least
7 tomorrow and Wednesday.

8 ADMINISTRATIVE LAW JUDGE: All right. Dr.
9 Tweeten, what is your availability?

10 DR. TWEETEN: My current plan is to be here
11 all day tomorrow.

12 ADMINISTRATIVE LAW JUDGE: All right. That's
13 all day tomorrow.

14 DR. TWEETEN: But not necessarily Wednesday,
15 unless I'm absolutely forced to that schedule.

16 ADMINISTRATIVE LAW JUDGE: All right, but not
17 necessarily Wednesday. We may -- I agree with you, Mr.
18 Moody, I would like to have Dr. Folwell have opportunity
19 to ask questions of the current witness, but then we may
20 not be able to complete the cross-examination of him
21 before we interrupt that to hear Dr. Tweeten's
22 testimony. We'll just have to see how it goes. Okay,
23 good. Dr. Jekanowski...

24 MS. DESKINS: Judge Clifton, one of the
25 procedural manner.

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1 ADMINISTRATIVE LAW JUDGE: Yes, Ms. Deskins?

2 MS. DESKINS: On the notice, there were other
3 proposals in there, including 2 through 10, and I'm
4 wondering if we can find out if there's anyone here who
5 wants to testify to those proposals and see when they
6 would be available to testify.

7 ADMINISTRATIVE LAW JUDGE: All right, that's
8 good. All of you probably notice the handouts that are
9 available in the boxes as you come in and on the last
10 page of that handout there are proposals, 1 through 10,
11 and on the next page there's also a proposal 10 that we
12 identified in Portland, should actually be marked as 11.
13 So with regard to those 11 proposals, is there someone
14 here who will be able to testify concerning those? Mr.
15 Moody, do you know?

16 MR. MOODY: Yes, Mr. Lonsing, L-o-n-s-i-n-g.

17 UNKNOWN: L-e.

18 MR. MOODY: L-e?

19 MS. DESKINS: Your Honor, I had asked around
20 about that. I've asked both Mr. Monahan and Mr.
21 Carswell and apparently they are not here today.

22 ADMINISTRATIVE LAW JUDGE: All right. Now,
23 the name you said, Mr. Moody, sound a lot like the name
24 that's printed in the Federal Register above the
25 proposals. Is that the name, L-e-n-s-e-i-g-n-e?

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1 MR. MOODY: Yes, it's just that I can't spell,
2 Your Honor.

3 ADMINISTRATIVE LAW JUDGE: All right. So what
4 is the first name of the gentleman with that as his last
5 name?

6 MR. MOODY: Leroy.

7 ADMINISTRATIVE LAW JUDGE: All right. And do
8 you know when he'll be available?

9 MR. MOODY: I think we're probably thinking of
10 later in the week, Thursday or Friday.

11 ADMINISTRATIVE LAW JUDGE: All right. And
12 then I believe the last proposal was authored by a
13 gentleman who will be coming here for his cross-
14 examination, if I remember correctly. All right. Okay.
15 Is it too late in the proceedings for us to hear from
16 someone on these ten proposals Thursday or Friday? Ms.
17 Deskins, do you believe that's a little late in the
18 proceedings for us to hear those ideas?

19 MS. DESKINS: We don't mind. We just want to
20 make sure people have an opportunity if they want to and
21 also from the schedule and I know Mr. Monahan and Mr.
22 Carswell have witnesses they want to get on and we just
23 want to make sure that everyone has an opportunity,
24 including people that want to talk about other
25 proposals.

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1 ADMINISTRATIVE LAW JUDGE: All right. Very
2 good. I hate late nights because I really do think it
3 affects the quality of our work the next day. People
4 get tired and they get irritable and sometimes they
5 fight the more, which makes my job harder, so I hope we
6 don't have to go too late, but we will go late tonight
7 if necessary to finish cross-examination, at least by
8 Dr. Folwell.

9 MR. MONAHAN: Your Honor?

10 ADMINISTRATIVE LAW JUDGE: Yes?

11 MR. MONAHAN: Brendan Monahan.

12 ADMINISTRATIVE LAW JUDGE: Mr. Monahan?

13 MR. MONAHAN: As long as we're talking about
14 schedules, there are two points that I should probably
15 bring up. First is that Mr. Christensen [ph], Rod
16 Christensen, is only available tomorrow, so he -- we
17 would need to conclude his testimony, which is going to
18 include direct testimony regarding miscellaneous
19 provisions in the proposed order. I also don't know
20 what Your Honor has concluded with respect to the issue
21 of time allotments. I think that with the conclusion of
22 Dr. Folwell's testimony, there is about four hours of
23 direct testimony left in the proponent's case. There
24 may be a couple hours of cross-examination, but I throw
25 that out at Your Honor for the calculations as to how

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1 the rest of the proceedings and witnesses and time
2 allotments should be in.

3 ADMINISTRATIVE LAW JUDGE: Okay, thank you.
4 I'll keep that in mind. It sounds to me that we may
5 have to reserve tomorrow primarily for Mr. Christensen
6 and Dr. Tweeten, but we'll revisit that in the morning.
7 And thank you for throwing that into the mix. All
8 right, now. It's 4:27. Dr. Jekanowski, you may resume.

9 DR. JEKANOWSKI: Okay, thank you. I forget
10 exactly where I stopped on the slide, so let's start
11 again with this slide. A little recap here.
12 Implications for having a market -- markets for base.
13 In other words, implications of base having value. It's
14 clearly a new cost of operation for some growers. It
15 will upset previous financial plans. I recall now I did
16 mention that growers that required to purchase base
17 simply to honor previous contracts that they're bound
18 to, they could get squeezed. If they can't afford the
19 base, they might be forced with deciding I have to
20 renege on their contract or purchase an asset that is
21 more than they can afford. If prices do not increase
22 from the hop marketing order -- in other words, if the
23 saleable isn't set lower than current production, those
24 higher costs, I think, almost certainly will force some
25 producers out of business and at least my understanding,

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1 based on this analysis I present before you, is that the
2 most efficient growers, those who've expanded the most
3 recently and perhaps those who have invested in high
4 alpha hop varieties, they are most vulnerable and I
5 think that's -- aside from the inequity of that, I think
6 it's also a real resource misallocation within the
7 market that will be a direct result of this marketing
8 order. And then finally, I think this new cost of
9 leasing or -- and/or purchasing base, will almost
10 certainly compete with other investments resulting in
11 less capital being available for new equipment,
12 different varieties, other business ventures. As I
13 pointed out earlier, if one grower's faced with having
14 to pay a million dollars just to maintain his last
15 year's production, that's a million or \$900,000 that he
16 could've used for other more productive assets, I would
17 submit. Okay. Moving on to slide 31. I think clearly
18 there's winners and losers as a result of this marketing
19 order and they're pretty easy to identify. The short
20 term winners are, just based on my hypothetical examples
21 I presented to you, are producers with sharply declining
22 production, because they receive base in excess of their
23 true production trend, so they're winners. I think
24 foreign producers are certainly winners. And that would
25 include China, Europe, and possibly new growing regions.

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1 You know, I asked Dr. Folwell this morning if anybody 15
2 years ago could've predicted that Argentina or Brazil
3 would've been nearly as large in soy bean production as
4 they are now, and I don't think anybody could've and I
5 think that illustrates that sometimes we can be
6 confronted with changes in technology and increased
7 investment in regions that we never even thought as
8 vital productions regions, so I just throw that out
9 there, as well. Now, the losers from this proposal.
10 Clearly, there's a long list of losers. New growers
11 with no production history, they'll be essentially
12 crowded out entirely, or have to, I guess, buy base to
13 enter. Growers with recent investment in high alpha
14 hops. Their production is going to be cut and they'll
15 be forced -- and/or forced to buy base to maintain their
16 production. Excuse me. Growers with stable alpha
17 production, because even them, at a 55 percent saleable,
18 they're certainly going to be restricted in what they
19 can market and have to buy base to make up the
20 difference. Growers with expanding production. That's
21 what my hypothetical example worked through. And I
22 think growers with contractual commitments. Again,
23 they're going to be losers because they're going to be
24 faced with the choice of either reneging on those
25 contracts when the base is cut to 50 percent or even 75

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1 percent, or buying new base in order just to honor those
2 contracts. So I think growers with contractual
3 commitments are clear losers under this proposal. And
4 just to kind of recap here, main points of this whole
5 previous analysis is that base will be widely sold and
6 traded and that's by design of the marketing order.
7 That will happen. As my simple analysis showed, a
8 saleable of less than 75 percent, possibly much less
9 than 75 percent, will be required for any restriction on
10 total supply. But even at 75 percent, even is the
11 saleable is set at 75 percent, hypothetically, that
12 would imply, by my analysis, adequate base being
13 available to ensure production at 2002 levels. But
14 steady and expanding growers must, as a result, purchase
15 or rent base from other growers just to maintain their
16 output. Alpha producers would see higher costs as a
17 result of having to purchase a base, but again, no
18 increase in price if supply isn't reduced. And I think
19 the burden, as a result of these characteristics of the
20 proposal, the burden is placed disproportionately on --
21 I'll call them efficient producers, being a -- that's
22 what an economist would call them. A producer who has
23 increased production over time, a producer who is
24 invested in new higher-yielding varieties. Again, I
25 don't know -- I can't claim a lot of knowledge about the

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1 hop industry per se, but from an economist's
2 perspective, we would consider those to be the efficient
3 class of producers. And again, I think that very fact
4 really illustrates the resource effects, the
5 misallocation of resources within the industry, which
6 ultimately is going to decrease competitiveness of the
7 US industry vis-à-vis their worldwide competitors. And
8 ultimately, you know, nobody's a winner from that. The
9 entire industry loses. Moving on to slide 33. You
10 know, I think it's also worth pointing out that this
11 proposal probably hurts small growers even more than
12 large growers and I'll explain why. First of all, with
13 a restriction on the saleable, a small grower will have
14 little opportunity for growth. And as I sort of worked
15 through my analysis, I hoped to point out that the price
16 of the allotment base will be determined by the
17 willingness and the ability to pay for that base. We
18 don't know what that price is going to be, but that's --
19 those factors are what's going to give it its value in
20 the market. Certainly, some growers might not be able
21 to afford necessary base, but others will. And I would
22 surmise that the large growers with scale economies,
23 more efficient production, perhaps, and the ability to
24 spread production costs over a larger base of fixed
25 assets will have a greater ability to pay for base than

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1 the smaller producers who might be operating at a lower
2 economy scale. And as a result, the price could
3 increase beyond the reach of small growers, precisely
4 the people who, my understanding is, this marketing
5 order is hoped to help or to preserve. So clearly,
6 contrary to marketing order intent. I want to talk just
7 briefly about the aroma -- or about aroma hops and just
8 to illustrate that in the proposal there seem to be some
9 statements that imply that, you know, that the aroma
10 hops are in balance and this proposal will preserve that
11 balance by giving the -- that excess allotment to hops
12 that are produced at less than 10 percent alpha. Yeah,
13 at less than 10 percent alpha. Just a few industry
14 facts just to put out there. By Hop Grower of America
15 estimates, about 40 percent of US aid which is devoted
16 to aroma hops accounting for about 26 percent of
17 production in terms of pounds, and some estimates place
18 domestic usage at about 80 to 90 percent for aroma hops.
19 I think we also learned from testimony in Portland and
20 also just from sort of industry, basic industry
21 knowledge, that a large percent of aroma hops are
22 contracted directly grower to grower, which I would say
23 is a healthy aspect of that market. And some of those
24 users are not solely concerned with alpha content in
25 price. In fact, there's other characteristics -- again,

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1 my understanding of aroma hops is that there's other
2 characteristics besides alpha that give them value in
3 the market. But if we kind of think this through
4 logically, if you're still regulating aroma hops based
5 on alpha composition, or based on alpha production, it
6 seems to me that would provide -- that stand the risk of
7 upsetting some of the conditions that currently balance
8 that market. For instance, clearly, there'll be
9 incentives to try to produce hops with lower alpha
10 content, aroma hops with lower alpha content, which
11 could have fundamental effects on the availability of --
12 produce hops with -- aroma hops with lower alpha
13 content. I'm not sure if I said that correctly the
14 first time. And I think that could have effect on the
15 availability of different varieties and really affect
16 the conditions that have led to the current balance in
17 this -- in the aroma hop category. It's apparent that
18 US brewers import domestic -- or, I'm sorry, US brewers
19 import similar quantity of aroma hops to what they
20 sourced domestically, which I think also shows that they
21 have access to world markets and the aroma hops are
22 available on world markets and could be substituted --
23 substitutable. And again, sort of the key point here is
24 that, at least, in my discussion with hop growers and
25 with people in the industry, demand and supply appear to

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1 be in balance. The level of contracting is high and
2 prices have generally increased from the mid-1990s into
3 the future, so anything -- any tool that stands the risk
4 of regulating the production of aroma hops, no matter
5 what perceived safety valves are in there, runs the risk
6 of upsetting this balance, I would submit. Moving on --
7 and actually, I already talked through most of these in
8 my previous slide, but again, aroma hops are currently
9 in balance. I believe that a marketing order will
10 directly interfere with this balance because, you know,
11 production is substitutable at the grower level and at
12 the marketing level, as well, with the availability of
13 imports. Regulating aroma hops based on alpha content,
14 which is -- my understanding is a characteristic that
15 typically doesn't even provide the value for aroma hops.
16 Regulating aroma hops based on this alpha content could
17 affect the types and varieties of aroma hops planted to
18 the disadvantage of the true market needs that are
19 typically used to guide the plantings of these different
20 varieties. And I think that it's also pretty clear that
21 a marketing order will create uncertainty among buyers
22 over the future availability of growers to honor
23 contracts for all of the reasons that I pointed out in
24 my previous hypothetical examples. And whenever you
25 increase uncertainty -- in fact, that likely decreases

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1 the incentives for buyers to lock themselves into a
2 contract that they're not sure if it's going to be able
3 to be fulfilled. So I think that's an important point
4 to bring out, as well. Moving on to slide 36. I think
5 it's worthwhile just, you know, to think briefly about
6 whether these equity or resource misallocation concerns
7 can be fixed. Are there any ways to modify the proposal
8 to get rid of some of those inequitable outcomes, and I
9 think it's pretty unlikely. I think the very nature of
10 this type of program, you know, makes that unlikely.
11 One idea might be to use only the most recent year to
12 set allotments and then, you know, we can imagine that
13 that might remove some of this excess allotment that's
14 going to be on the market and bring the initial base
15 more closer to a competitive equilibrium. As a result,
16 the restriction on saleable would certainly apply
17 equally to all growers. I mean, that would be a real
18 way of, you know, sharing the burden, I guess, so to
19 speak. But it certainly is -- it's a politically
20 unpopular strategy and there are reasons why I agree
21 that it might not be appropriate and that's what if a
22 grower had one bad year? You're going to penalize him
23 because of bad luck. Moving on to slide 37. Some ideas
24 of maybe fixing the equity concerns. In comments to
25 USDA, I noted that some people suggest well, what if we

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1 strictly forbid the sale and transfer of base, just
2 whatever. Say that it's illegal to sell base, won't
3 that eliminate the market? But I don't think that
4 that's realistic, as I pointed out, for the reasons I
5 pointed out in my earlier testimony, base will always
6 have a value and transactions are private. How -- you
7 can't really police what people do in private. And if
8 somebody's willing to pay for base, they're going to
9 find a willing seller. I don't think there's really any
10 other alternative more efficient method of allocating
11 base besides price, I mean, it should, I guess, if
12 you're forced to have to pay -- have a market for base.
13 A grower's willingness and ability to pay should guide
14 that market. It still seems to be the most efficient
15 allocation mechanism. I think tighter restrictions
16 would mean even more government regulation and policing
17 of this market, which would be unfortunate and
18 unpopular. You know, I would just, again -- it's hard
19 to precisely work through the implications, but I think
20 it could lead to an industry under-supply of hops
21 despite the best efforts of the hop administrative
22 committee, because without being able to sell base,
23 certainly growers would have little incentive to
24 transfer it to others. So some growers, those growers
25 who are constrained would really be constrained because

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1 they would have no way of receiving base from others.
2 And on that note, I think even the bona fide effort
3 requirement, and again, I'm not a lawyer, so I can't
4 claim to know the true implications of or meaning of or
5 intent of bona fide effort requirement, but my
6 understanding is that even that can interfere with
7 market balance by creating basically a use it or lose it
8 mentality. So some growers, who might have had no
9 intention of increasing their hop production might say
10 well, I have this base and if I don't use it, I'm going
11 to lose it so I'm going to at least produce up to my
12 maximum base, which again, interferes -- at very least,
13 it interferes with the ability of the hop administrative
14 committee to estimate how saleable will affect the true
15 supply. Moving on to next topic. I want to talk
16 briefly about new growers and the implications for new
17 growers and barriers to entry. Just to make sure again
18 we're all on the same page, I'm going to read real
19 quickly -- this directly out of the proposal, the
20 implications -- the provisions governing new growers.
21 "The committee annually shall make additional allotment
22 bases available in the amount of no more than one
23 percent of the total allotment base. 50 percent of
24 these additional allotment bases shall be made available
25 for new producers and 50 percent made available for

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1 existing producers" -- excuse me -- "provided that in
2 any year in which the current saleable percentage is
3 equal to or less than the previous year saleable
4 percentage, the committee shall not be required to make
5 additional bases available for ensuing market years." I
6 think even without being a lawyer, it's pretty clear
7 that that's a severe restriction on new growers and the
8 availability of new base to new growers, but again, I
9 think it's worthwhile to just sort of run a real quick
10 scenario here to see what this means, you know,
11 quantitatively. Again, return to my example where we
12 assume an allotment of 9.2 million pounds of alpha. And
13 assuming that somehow that becomes the long-term
14 industry base, one percent of 9.2 million is 92,000
15 pounds, 50 percent of which will be available for new
16 growers, in other words, 46,000 pounds will available
17 for new growers. Assume a new grower wants to produce
18 high alpha hops, 15 percent alpha yield at 25,000 --
19 2500 -- 2,575 pounds to the acre, that implies 401.5
20 pounds of alpha per acre is what he wants to produce.
21 The result of this restriction, I mean, clearly just by
22 simple math is that in the years when the committee
23 decides that base can be made available, and that's
24 making available roughly 115 acres to new growers, and
25 even that would still likely be subject to a saleable.

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1 Again, not knowing a lot about hops, to me that seems
2 very low based on my general knowledge of agriculture
3 and other agricultural industries, so I did a little bit
4 of digging and looked at the 1997 census of agriculture
5 that was done by the United States Department of
6 Agriculture. They report 149 hop farms, which from
7 testimony this morning, it appears to be way too high.
8 But be that as it may, 149 hop farms and using 1997
9 acreage implies that the average size of a farm is 290
10 acres, which I think is -- people in this room would
11 probably agree is a, you know, pretty severe
12 underestimate of the true average size of farms and
13 almost certainly below a minimum efficient scale. Just
14 to kind of return again to some text book results here.
15 Implications, industry-wide, of this type of marketing
16 order, again, higher costs for many producers,
17 disincentives to invest in capital to improve -- capital
18 improvements or technology, certainly incentive to
19 invest in higher yield in hops. I think it discourages
20 new farmers pretty clearly, because it increases the
21 barriers to entry. They're going to have to buy base to
22 enter or wait for that 115 acres that might be available
23 five years hence. And I think, also, it's pretty clear
24 that it will provide a signal to foreign producers to
25 increase output. With any restriction in domestic

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1 supply, that's a direct signal to foreign competitors to
2 increase output. And just, you know, for the record, I
3 think it's worthwhile noting that the -- basically,
4 these resource misallocation costs imposed by the
5 allotment program are also in addition to the
6 administrative costs, which -- that will also result and
7 they're somewhere in the range of -- we heard estimates
8 of 200,000 per year, though we don't know exactly.
9 We'll have a better idea of what the administrative
10 costs are, I guess, after the committee decides. Moving
11 on to slide 41, real briefly -- and I'm not going to
12 dwell on this because as we've heard so much about how
13 the last marketing order was a success, but just, you
14 know, stating for the record here that there was, in
15 fact, a similar marketing order -- similar anyway, in
16 place from 1966 to 1985, and my analysis of it -- again,
17 I wasn't here, I wasn't in any position to judge it back
18 then, for sure, but from what I've read and in talking
19 to growers and talking to USDA folks, I think it's
20 pretty clear that it was extremely controversial and it
21 was opposed in principle by the Reagan administration,
22 similar to the way, I guess maybe, the Bush
23 administration's policy principles also opposed these
24 types of programs in principle. But this was opposed in
25 principle 20 years ago, as well. My analysis is that --

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1 or my hypothesis is that it undersupplied the hop
2 market, especially following unexpected foreign crop
3 failures. Certainly, greed entered into it and there
4 was -- there were numerous law suits and administrative
5 burdens borne by USDA and the industry itself, fighting
6 over whether to increase the saleable in order to allow
7 new base to be issued. Clearly created a market for
8 allotments and imposed costs on many producers and I
9 think it's safe to say inefficient transfers of wealth
10 within the industry. Created barriers to entry. And I
11 think it, you know, another thing hasn't been mentioned
12 here, but I think it's important to point out, that I
13 would guess that it also added to the management burden
14 for producers. You know, no longer is it enough to just
15 monitor the market for hops, now you have to worry about
16 how best to use your base allotment. Do you produce
17 hops yourself, or do you sell your base to somebody
18 else? Do you transfer, do you trade, do you lease?
19 It's just another layer of management burden that's
20 placed on the industry. Just a real quick analysis
21 here. You might ask why do I think the hop market was
22 undersupplied and I can't offer any type of a
23 complicated analysis to prove this, but you know, as an
24 economist, I -- when you look at prices increasing
25 rapidly at any point in time, or over any point in time,

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1 you don't necessarily view that as a healthy market. I
2 would view that as a restricted market. Maybe it was
3 restricted because of German crop failures, maybe it was
4 -- or it was undersupplied because of German crop
5 failures, but certainly higher production might've
6 brought that market more into balance. Sustained
7 increases of the magnitude we saw in the late 1980s, I
8 think just are not possible. At some point, markets
9 have to adjust. It's kind of like a coiled spring that
10 just keeps getting pressed down. Eventually it's going
11 to pop back and the markets must adjust. And if, in
12 fact, industry -- the industry was undersupplied, well I
13 would say that total industry revenues were sacrificed
14 as a result. Some producers could've maximized their
15 revenue by increasing the production during those
16 periods when prices were really, really increasing like
17 crazy, but the -- marketing order restricted that. As a
18 result, again, greed entered into it, lawsuits ensued,
19 and you know, what happened was that production couldn't
20 respond to the -- to market signals. And I think in
21 previous testimony, we heard and widely acknowledged
22 that greed was a problem in the last marketing order and
23 that's what led to maybe prices rising too fast and then
24 saleables set too high. Greed was part of it, but I
25 have yet to hear a good way to prevent greed from

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1 entering into the proposed marketing order. I think
2 it's human nature. What I would like to do now --
3 excuse me, I felt slightly out of -- okay. Another --
4 you know, I just sort of throw this out as something to
5 think to about. You know, we hear a lot of reference to
6 the need to for, you know, a hop marketing order to
7 bring stability to the market, to bring stability to
8 prices, even if the intent isn't to increase prices,
9 it's all about stability. Well, we haven't really heard
10 a good definition of how you -- how exactly you define
11 stability. One measure of stability is the coefficient
12 to variation and this is at the mean of the data. It's
13 basically mean divided by the standard deviation. And
14 just to throw it out there that even though the previous
15 marketing order is sort of held up as a big success, in
16 fact, if you look at -- if you measure this by this
17 measure of stability, prices were actually more variable
18 during the marketing order than they were after the
19 marketing order and I admit and what's going on there,
20 clearly, they're variable in one direction. They're
21 going straight up. But again, I submit that that's not
22 necessarily a health industry. And when we got rid of
23 the marketing order, certainly there was some
24 fluctuation, but over time this coefficient to
25 variation, this measure of variability is actually much

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1 less than prior to the marketing order and that's aside
2 from the fact that -- I think, you know, the years '87,
3 '88, when prices dipped down there, I think part of that
4 is just a function of the market having to readjust from
5 this severely restricting marketing order being removed,
6 so I don't think it's really quite even fair to judge
7 the decline in prices right after the marketing order as
8 a function of the removal of the marketing order. I
9 mean, it's more a lag response to the markets having to
10 return to equilibrium after having been so severely
11 constrained. The market today -- the factors
12 complicating the marketing order -- even if you accept
13 that the marketing order, previous marketing order
14 worked, we can't get away from the fact that the
15 industry is different today, so what worked 25 years ago
16 might not work, or least might not work as well today.
17 And some of the factors that I think are important is,
18 you know, increase -- is the fact that today versus 25
19 years ago, most people would agree that we -- we're
20 living a global economy with increased trade, generally
21 easier sourcing of goods and materials worldwide, and
22 multi-national brewers and processors. Again, this just
23 increases the ease with which hops can flow across
24 international borders. I think we are seeing -- and
25 this has come out in testimony, a loss of alpha

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1 production base to some foreign producers, including
2 China or perhaps the EU, Eastern Europe, and others, so
3 there are more competitors out there from an
4 international standpoint. I think we've seen processing
5 techniques that enable prolonged storage, which again,
6 storage is typically viewed as a way of managing risk in
7 a way of allowing producers and brewers and all market
8 participants to sort of dampen out the large changes in
9 price. Basically, you can hold your inventory when
10 prices are low and sell it when prices are higher. We
11 certainly have increased production of high yielding
12 varieties, at least, from what some people have told me
13 during the last marketing order you basically only had a
14 couple of varieties. Maybe that's an
15 oversimplification, but I think we certainly have new
16 varieties available today that weren't available 25
17 years ago and it will affect the ability for a hop
18 marketing to work. And again, I believe the technology
19 is fully transferable overseas. So even if you accept
20 that maybe with current technology, China can't compete
21 with the US in terms of hop production, I -- it's my
22 belief that there's basically nothing stopping them from
23 being able to compete at one -- some day and that higher
24 world prices will be the incentive for them to transfer
25 this new technology, or to increase their own

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1 production.

2 ADMINISTRATIVE LAW JUDGE: Yes, let's
3 change...

4 ***

5 [Off the Record]

6 [On the Record]

7 ***

8 ADMINISTRATIVE LAW JUDGE: All right, we're
9 back on record at 5:01. You may resume.

10 DR. JEKANOWSKI: Okay. Thank you. Moving on,
11 I think this slide kind of speaks for itself, to some
12 degree. It -- this is data from the United Nations, FAO
13 stands for Food and Agricultural Organization. It's the
14 only real source I could find for international
15 statistics of hop production. And these are just
16 acreage shares, so it's not considering alpha, it's just
17 simply acreage of hops in different countries, and we
18 can look at what's happened over time, just over the
19 past 10 years. We see a little bit of an increase in
20 the German share, and these are again, shares.
21 Increased in Germany. In the US, we were kind of
22 increasing a little bit through the early to mid-90s and
23 then leveling off and then declined somewhat. But to
24 me, the one that's really stunning is Asia developing
25 and that's China, essentially. They've increased

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1 production tremendously over the past decade and I would
2 say there's no reason to expect them to stop producing
3 or to stop growing their world share over time. So when
4 you're talking about restricting supply in the US
5 market, it's just going to have less and less of an
6 effect on world prices as you go forward. It's just --
7 it can't work, in my opinion. So -- all right, so why,
8 then, would we even consider a marketing order? I
9 thought it was worthwhile to -- even though I noticed in
10 direct testimony the justification for a marketing order
11 sort of changed a little bit from the original proposal
12 that was submitted to USDA that -- about why a marketing
13 order is needed and I didn't realize at the time that
14 the justification might've changed, but I thought it was
15 worthwhile to sort of go through the problem statements
16 that were clearly identified in the original proposal
17 and kind of address those in sequence, or give my
18 analysis of them. Problem number one, brewers have
19 moved away from long-term contracts. We've had a lot of
20 talk about that and that may be true over recent years,
21 but my response to that would be that the soul in that
22 position, in other words, contracting, is in fact, a
23 signal of market needs and the degree of elasticity.
24 And I have a -- I'm going to flip ahead just briefly
25 here. This was a chart that was actually in the

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1 original proposal. Let me get it. Okay. The way I see
2 it, the degree of contracting, is in fact, a signal of
3 market needs. If you take a look at this chart, I think
4 you can clearly see that as the degree of contracting
5 declined, especially in recent years, from 1999 through
6 2001, it's also matched with generally a decline in
7 production over time, as we would expect. If you can't
8 -- if you don't have market for your hops through a
9 contract, maybe it shouldn't be produced in the first
10 place. And then, I'd also just like to point out that
11 the degree of contracting was -- has been as high as 98
12 percent in 1994, 90 percent in '92, it pretty much
13 hovered right around upper-80s to 90 until 1997 before,
14 for some reason, jumping way up, but I would say that
15 jump to 122 isn't necessarily a good thing for the
16 industry, but the degree of contracting, I would submit,
17 hasn't declined precipitously after the last marketing
18 order. Certainly, we had a couple of years of lower --
19 of a decrease in the amount of contracting, but that's a
20 fairly recent phenomenon, so any recent decrease, I
21 don't think should be necessarily attributed to not
22 having a market order.

23 ADMINISTRATIVE LAW JUDGE: I'm sorry. I don't
24 understand how you can get higher than a hundred
25 percent.

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1 DR. JEKANOWSKI: You know, I'm not entirely
2 sure, either. This is a Hop Growers of America data. I
3 assume that people contracted for more than they knew
4 they were going to produce.

5 ADMINISTRATIVE LAW JUDGE: Mr. Roy, you
6 indicated you could explain that?

7 MR. ROY: I'd like to question him on cross-
8 examination, rather.

9 ADMINISTRATIVE LAW JUDGE: Oh, okay.

10 MR. ROY: I'd rather...

11 ADMINISTRATIVE LAW JUDGE: Oh, all right. All
12 right, go ahead.

13 DR. JEKANOWSKI: Okay. Thank you. Just to go
14 back a second, here. Again, we should also just take
15 note that some of the surveys are mandatory, so even the
16 numbers that are presented to some uncertainty, and you
17 know, the fact that the decreased contracting or a lack
18 of contracting is being associated with the need for a
19 marketing order. To me, it best represents an attempt
20 by the proponents to essentially, hold the buyers
21 hostage, saying that we're going to, you know, well,
22 we're going to be producing less in future years, so you
23 better contract with us now. I guess, hypothetically,
24 that might increase contracting, but other than that, I
25 see no real reason to assume a connection there between

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1 a marketing order and the degree to which the industry
2 is contracting. The degree to which contracts are
3 entered into. But I would also submit, again, as we
4 said over and over that restricting supply will also
5 force brewers to search for alternative sources of
6 supply. Maybe to contract less, in fact, because of the
7 increased risk of future availability of hops. Okay,
8 problem two. It was stated as no structure currently in
9 place to manage the supply of hops, as the fixity has
10 been the stimulus for continued production. No price
11 spikes in over a decade since German crop failures are
12 now a rarity. I think I know why this -- at least the
13 last sentence of this problem was probably dropped from
14 the justification, but in general, my response to that
15 would be that economic theory and historic experience
16 shows that efforts to manage supply adversely affect
17 industry efficiency in productivity. Again, I think
18 this is basic text book industrial organization theory.
19 Monopolists are -- monopolists and cartels are known to
20 be inefficient and to be notoriously poor at allocating
21 resources and setting market supply. I would say that
22 asset fixity is a problem throughout agriculture, but
23 the variation in hop acreage and production at least
24 shows to me that the supply is not fixed. There is
25 supply response, And we've also learned that today

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1 growers can plant hops and get almost a full crop in the
2 same year. If anything, that increases the degree to
3 which market -- to which producers can supply -- can
4 respond to market signals. I clearly hold the absence
5 of German crop failures as well outside the domain of a
6 marketing order and plus, I would say that crop failure
7 has only increased volatility, precisely what the
8 marketing order is intended to reduce. It certainly
9 would increase volatility since -- if you're restricting
10 supply and you can't predict future crop failures, it
11 leads to unwarranted price spikes. I would say that no
12 committee can accurately predict a crop failure. Again,
13 increasing the potential for market undersupply if a hop
14 marketing order is in place, because basically, a crop
15 failure can only reduce supply, so if you go ahead and
16 you set the saleable at some level, then you're faced
17 with a German crop failure, you're -- automatically
18 you're undersupplying the market. And I think the
19 current German crop failure show [sic] that these events
20 do, in fact, still occur. Problem three. The strong
21 dollar was mentioned and is putting American growers at
22 a disadvantage. And again, the response there is pretty
23 clear. A strong dollar hurts all export-oriented
24 industries, but a marketing order with supply
25 restrictions can't fundamentally address this concern.

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1 There's -- it may be true that a strong dollar has
2 marginally affected competitiveness with some other
3 countries, but restricting supply in the US isn't the
4 response to that. And at least I found from the data of
5 the hop growers association, that the hop exports have
6 generally been growing despite the stronger dollar,
7 which to me sort of raises a question about whether
8 American growers have really been put at a competitive
9 disadvantage. And finally, recent trends have show a
10 dramatic decline in the dollar's value, which should,
11 you know, obviate this problem and ultimately help
12 exports. And -- but ultimately, currency fluctuations
13 can't be addressed by a marketing order and it has --
14 they have no place in a marketing order proposal, I
15 would say. And that's just a chart of the value of the
16 dollar. This is against -- this is the real value of
17 the dollar against all major currencies, not just
18 Germany, but all major trading partners. And clearly,
19 the decline since mid-2001, or 2000, is certainly clear.
20 Okay, here we go. Problem four. Throughout the -- and
21 this, again, was stated right -- in the proposal.
22 "Through the internet and email contacts worldwide,
23 routinely provide valuable information on market demand.
24 Growers today are better informed on market decisions
25 than every before, however, no central authority exists

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1 to use this information to manage the industry as a
2 whole. You know, maybe it's just a philosophical
3 difference here, but I would say that generally
4 speaking, and I think most economists would agree that
5 greater availability of market information is rarely
6 cited as a need for supply in management. Usually that
7 implies that the market, the free market, is even better
8 at working than when you have less information. And I
9 would also say that no central authority will ever be
10 able to accurately predict market supply and demand
11 conditions in today's world economy. And if the most
12 efficient and accurate method for growers to use --
13 method is for growers to use this increasingly available
14 information that the proponents note is out there. Now,
15 one other issue -- this wasn't cited as a problem, but
16 it was certainly mentioned in the proposal that "grower
17 problems are compounded by the lack of an exit strategy
18 from the industry." We heard over and over again that
19 the value of used hop equipment is almost non-existent
20 and whatnot, but I think that this statement really --
21 it seems to illustrate, possibly, the real intent of
22 this marketing order. I -- a marketing order like this
23 would certainly offer an exit strategy if growers wanted
24 to sell base and be paid to reduce their production and
25 be paid to exit the industry. And that transferable

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1 asset allotment base would provide that mechanism. But
2 again, the reality is that such a strategy simply of
3 transfer of wealth between producers where existing
4 efficient producers are forced to pay those who are
5 unable or unwilling to compete in the market. Again,
6 just to sort of recap here a list of winners and losers
7 as a result of this marketing order, as I see it.
8 Again, winners are growers with already declining
9 production and overseas producers as I mentioned over
10 and over again. Losers -- I'll just read these because
11 I think addressed everyone already. Losers, any grower
12 that maintained or expanded production, growers with
13 contractual obligations that they are unable to fulfill,
14 small growers hoping to become larger, non-growers
15 hoping to enter the industry. Aroma producers are
16 potential losers as regulation upsets an already
17 balanced market. Small breweries, I think, are
18 potential losers as they're faced with higher costs and
19 possibly less availability of different varieties and
20 less availability of hops. Buyers with unfulfilled
21 contracts. Buyers are losers is they're, you know, if
22 they're faced with unfulfilled contracts on behalf of
23 their suppliers. I think consumers are losers as prices
24 rise and we heard testimony this morning that maybe the
25 rise in prices is miniscule and I have, you know,

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1 nothing to verify or contradict that, but I think at the
2 margin, it's still an important effect on price and it
3 can also affect new product introductions. If this
4 marketing order affects the varieties of hops available
5 and affects the varieties that are produced in the
6 market, you know, new product introductions can lag and
7 ultimately, everybody loses from that. And then,
8 finally tax payers and USDA are also losers as tax
9 payers -- as USDA faces new administrative burdens and
10 the potential for litigation, which again, that's just a
11 lesson from the last marketing order. I also -- I just
12 wanted to go through a couple other issues real quick
13 here. I also -- I can't claim to be a, you know,
14 necessarily an expert in spearmint or cranberries, or
15 other industries in which there are marketing orders,
16 but I thought it would be useful to just take a really
17 quick look at those industries that are regulated by
18 marketing orders and you know, think about whether or
19 not they've been successful. In spearmint, an allotment
20 program has been operating since 1980. Now, spearmint
21 is a little bit different from hops in that substitutes
22 for US spearmint oil include foreign production and
23 domestically produced peppermint, at least at some
24 degree, they compete for the same market. But the way I
25 see it, the results of the spearmint allotment program,

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1 which again has been repeatedly pointed to as the
2 program that's working and which we want to, you know,
3 model the hop marketing order after and I'll put up some
4 charts in a minute that the results include stagnant or
5 declining exports, increased availability of the
6 competing product, that being peppermint, increased
7 imports of peppermint and spearmint, and a very dubious
8 effect on grower prices. And this chart, again -- this
9 is chart 55, or slide 55 -- this just shows the
10 production of spearmint and peppermint. This is again,
11 this is just the USDA National Ag Statistic Service
12 data, and we can look at the period prior to and after
13 the marketing order. We see clearly that spearmint
14 production, highly regulated, or restricted, has been
15 roughly flat since 1980, but peppermint production, this
16 potential substitute, clearly has been trending higher.
17 And again, the spearmint order has no way of regulating
18 peppermint, but it just shows the substitutability of
19 products. Let's take a look at exports of peppermint
20 and spearmint. Spearmint, again -- I didn't have data
21 going back real far. I apologize for that, but we can
22 certainly see what's happened since the spearmint
23 marketing order went into effect. Exports of spearmint
24 kind of bounce around pretty level at about, I guess
25 that's a million pounds. Exports of peppermint have

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1 done nothing but trend upward. I'd rather be in the
2 industry with the increasing exports, I think. Imports
3 of spearmint and peppermint, I think this one's pretty
4 dramatic. Again, we historically imported very minor
5 quantities of either peppermint or spearmint, but since
6 -- clearly, since the marketing order -- and there was
7 maybe a lagged effect here for markets to adjust and for
8 buyers to find alternative sources, but I think the
9 imports -- the growth in imports of those two products
10 is -- you know, speak for themselves. Quite dramatic.
11 So now, let's look at grower prices, if the true measure
12 of success is grower prices of spearmint. Well,
13 certainly, there's still a lot of fluctuation in grower
14 prices of both spearmint and peppermint. But it at
15 least appears to me that the price for spearmint, the
16 most recent prices, I think that's 2003, are about the
17 same as they were in 1980 when the marketing order came
18 into effect. Certainly they went up, but right now
19 they're back -- right back to where they are, which I
20 think illustrates again, with all of -- put that
21 together with the rise in imports that I showed earlier,
22 and I think it's pretty clear that you can't restrict
23 these markets and not expect a response from
24 competitors. And I also note that actually peppermint
25 prices are, at least according to USDA, now higher than

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1 spearmint, for what that's worth. Another thing I
2 thought was quite interesting and rather -- when I was
3 doing a little bit of research about spearmint marketing
4 order, again, admitting not to be an expert on
5 spearmint, I thought it was worthwhile to look at the
6 Federal Register to see, you know, how they set the last
7 saleable and I found the most recent one and this is
8 from the final rule, I think, for the saleable, probably
9 for last season, I forget exactly. But this is written
10 right into the Federal Register and I just want to read
11 this for you here, that "when the order became effective
12 in 1980, the United States produced nearly 100 percent
13 of the world's supply of Scotch spearmint oil of which
14 approximately 72 percent was produced in the regulated
15 production area in the far west. The far west's market
16 share is a percent of total world sales has average
17 about 45 percent since 1990. Between 1996 and 2000, the
18 committee's marketing strategy for Scotch spearmint oil
19 centered around an attempt to regain historical share of
20 the global market. The committee has since refocused
21 its strategy. Although sales increased somewhat, the
22 far west's market share -- percentage of total world
23 sales did not increase on average." You know, I read
24 that -- we heard in testimony in Portland and maybe here
25 today that, you know, the committee will be able to

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1 manage its exports and still grow exports and remain
2 competitive -- well, it sounds to me like that was what
3 the members of the spearmint marketing committee order
4 also intended, but what happened? They watched their
5 market dwindle from nearly a hundred percent market
6 share down to 45 percent and now, as a result, they've -
7 - I read it that they've basically given up on worrying
8 about growing exports and worrying about world markets
9 and are conceding that -- and just concede that market.
10 So I find that fascinating. I couldn't make something
11 up like this, I mean, this -- I think this perfectly
12 illustrates the problems -- maybe we could -- you know,
13 the problems that are likely in the hop industry maybe
14 next year, maybe 10 years hence, but over the long run
15 going to bring into effect the same -- going to have the
16 same problems. All right, so that's spearmint. Again,
17 that was pointed out as one that works. Another
18 marketing order is cranberries. And cranberries
19 operates a little bit differently from these other
20 marketing orders in that -- at least, my understanding
21 is that growers vote every year whether or not to have
22 an allotment program, so in reality, I think 2000, the
23 year 2000 was the first year they had an allotment since
24 like, 1972 or some year much previous. But
25 nevertheless, as a result of low prices, they voted in

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1 an allotment. I set the initial saleable at 85 percent.
2 And the 2001 saleable was 64 percent. Now, with
3 cranberries, the most likely substitutes are imports
4 primarily from Canada. Maybe only from Canada. And as
5 a result, just like clockwork, just like we would
6 expect, based on basic economic theory, after the US
7 allotments were put in place, imports increased --
8 cranberry imports increased from Canada. We had growth
9 in Canadian production and like hops, there's a large
10 fixed investment in putting in a cranberry bog and once
11 those acres are in effect -- are in place, you know,
12 it's hard to get them out of production. And I also
13 heard -- and this is sort of anecdotal -- just from
14 talking to some people who administered the cranberry
15 marketing order, that as a result of the allotment, even
16 plantings in the US increased that year for future
17 harvest and again, like hops, or maybe even worse than
18 hops, it takes several years for cranberry production to
19 ramp up to full potential. And I -- these are just sort
20 of graphically shown what happened to imports of
21 cranberries from Canada after the allotments were put in
22 place in 2000, 2001. Canadian cranberry production,
23 despite, you know, cranberries are world market, as
24 well. Canadians were experiencing low prices, but
25 they've increased their production over time and I would

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1 say it was partially -- at least partially because of US
2 allotments in place. Okay, so just to sort of wrap
3 things up here. Conclusions and economic implications.
4 I think it's safe to say that history and historical
5 experience and economic theory clearly illustrate the
6 pitfalls of allotment-based supply controls and these
7 include long term harm to international competitiveness,
8 decreased innovation in technology adoption, burdensome
9 costs and constraints on efficient producers, and
10 inequitable transfers of wealth to others. We're almost
11 certain to see a market for allotments and a substantial
12 administrative burden, especially if the committee
13 under, overestimates true market conditions. If we get
14 any replay of what happened in the last marketing order
15 towards its end. A couple things -- I mean, these
16 aren't necessarily, you know, economic topics, but I
17 think they're worth discussion and they -- I think most
18 of these have not been discussed yet, but I think they
19 should. One -- you know, how are grower obligations
20 under existing contracts going to be managed, and I
21 don't know. Again, I'm not a lawyer and I -- but I
22 think that's something that needs to be considered.
23 Would a marketing order force growers to renege on
24 existing contracts? Committee representation, I think,
25 is important because, you know, as we know that the --

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1 you know, the brewing industry also has its own -- it
2 has its own interest in seeing the hop industry remain
3 healthful -- remain healthy and there should be some
4 talk about who gets to be represented on these
5 committees. We -- I guess last week we did talk some or
6 there was some debate about voting rights and defining a
7 grower and it's clear that that's still not at all
8 clear. Another issue that I think is worth discussion
9 is assigning alpha base using actual historic alpha.
10 Excuse me. And I'm just curious again, not in
11 necessarily knowing a lot about the industry, but I'm
12 wondering if that can be done with the right amount of
13 precision, and is there potential for cheating and abuse
14 and how does that affect how this marketing order is
15 administered. I really think, you know, there needs to
16 be a real honest and direct discussion about the
17 intended method to set saleable quantity and exactly how
18 market needs and supply will be forecasted. I don't
19 think it's sufficient to say that well, it appeared to
20 work 25 years ago, so it might work again today. And I
21 don't think it's -- I also don't think it's sufficient
22 to say that this something that the committee will deal
23 with after the marketing order's in place. I mean, this
24 really the heart of the marketing order, having -- being
25 able to provide some assurance that this committee will

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1 be able to accurately set a saleable quantity.

2 MR. MOODY: Your Honor, I've sat here
3 patiently for the last couple of hours and -- listening
4 to the presentation. I would ask that this witness
5 limit his remarks -- I realize he only has a couple of
6 slide left -- to actual testimony as opposed to
7 commentary and argument over issues that have not been
8 addressed.

9 DR. JEKANOWSKI: I'm sorry. I didn't intend
10 for this to be argument, but I thought it was just, you
11 know, issues that do need to be addressed that I think
12 are going to be difficult to be addressed.

13 ADMINISTRATIVE LAW JUDGE: Your objection's
14 noted, Mr. Monahan, but you may proceed...

15 DR. JEKANOWSKI: Thank you.

16 ADMINISTRATIVE LAW JUDGE: ...Mr. Jekanowski.

17 DR. JEKANOWSKI: Thank you. And I am almost
18 done here. I've got one slide left. Again, how
19 accurately can alpha be measured? And there -- this
20 does have economic implications, you know, we're
21 assuming from the outset that alpha can be accurately
22 measured and regulated, but as an economist, I would
23 like to know whether or not that can truly be done. And
24 finally, part of the operating costs of the marketing
25 order -- we did talk a little bit about that last week.

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1 So final thoughts, you know, a couple -- and these are
2 maybe a little bit philosophical, but I'll go through
3 them quick. On thing that I think is certainly true,
4 that once enacted, these types of programs are extremely
5 difficult to terminate. And it's not surprising why,
6 because if you have some growers who invested heavily in
7 purchasing base, they're not going to want to see this
8 market order go away, because if they do, they'll be --
9 they'll have a direct decrease in their -- in the value
10 of the assets that they hold. So once these thing are
11 put in place, you know, it's not an easy thing to get
12 rid of them and maybe that's what we've seen with the
13 spearmint marketing order despite it's questionable
14 results. I think that the potential for fraud and abuse
15 -- and this is an economic conclusion, that the
16 potential for fraud and abuse increases with the
17 rigidity of supply controls and it would -- we would
18 likely expect, you know, more litigation and industry
19 in-fighting, greed, hard feelings. I don't think that's
20 healthy for an industry. Handlers have tremendous
21 responsibilities under this order, which -- at least
22 from testimony last week, it appears to me, could
23 discourage direct sales to brewers for those growers who
24 now have learned that if they sell direct to brewers,
25 they're considerer handlers. It seems to me if that

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1 were asparagus, we would expect that that would
2 discourage direct sales to brewers. And then the last
3 thing, and this is just sort of editorial, or and -- you
4 know, but I'll throw it out. It's just something that
5 kind of struck me -- and I'm not a legal expert or a
6 lawyer, but it doesn't seem to me to be necessarily fair
7 to have growers vote basically on how wealth should be
8 redistributed in their -- within their own industry.
9 You know, I think that, you know, potentially, at least,
10 it's sort of the tyranny of the majority, if clearly
11 those who have vested interests in having base -- the
12 value of base increase are voting so that other growers
13 might have to pay them for that. It's just, you know,
14 my own observation there. You can take it for what it's
15 worth. And that concludes my direct testimony.

16 ADMINISTRATIVE LAW JUDGE: Thank you, Dr.
17 Jekanowski. Do you wish to have Exhibit 30 admitted
18 into evidence?

19 DR. JEKANOWSKI: Was that my presentation?

20 ADMINISTRATIVE LAW JUDGE: Yes.

21 DR. JEKANOWSKI: Yes, yes.

22 ADMINISTRATIVE LAW JUDGE: Is there any
23 objection to Exhibit 30 being admitted into evidence?
24 There is none. Exhibit 30 is hereby admitted into
25 evidence. Dr. Jekanowski, would you please identify the

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1 compensation that you have received for participating in
2 the work that you've done for the hearing and also, when
3 you identified Sparks, I'm not sure you actually gave us
4 a mailing address in Washington, D.C., so if you'd
5 actually give us the street and so forth, I'd appreciate
6 that.

7 DR. JEKANOWSKI: Gladly. I'll do that first.
8 Sparks -- mailing address is Sparks Companies,
9 Incorporated, 6862 Elm Street, E-l-m, Suite 350, in
10 McLean, it's M-little c-capital L-e-a-n, Virginia, and
11 the zip is 22101.

12 ADMINISTRATIVE LAW JUDGE: And do you maintain
13 a web site within the company?

14 DR. JEKANOWSKI: Yes, we do. And it would be
15 www.sparkskompanies -- all one word -- .com.

16 ADMINISTRATIVE LAW JUDGE: Thank you.

17 DR. JEKANOWSKI: Sure.

18 ADMINISTRATIVE LAW JUDGE: And your
19 compensation?

20 DR. JEKANOWSKI: Sparks is a private company
21 and we do work for a fee, as most private companies do.
22 I'm uncomfortable to say what my actual compensation is.
23 I think that's sort of business, you know, proprietary
24 business, but we were initially contacted by a hop
25 grower -- actually, by a lawyer retained by a hop grower

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1 to provide, you know, to provide an economic analysis of
2 how this marketing order could affect them and then over
3 time, you know, our -- that hop grower has enlisted or
4 coordinated support from other hop growers to pay our --
5 to pay my professional fee.

6 MS. DESKINS: Your Honor?

7 ADMINISTRATIVE LAW JUDGE: Ms. Deskins?

8 MS. DESKINS: Under the rules of practice, I
9 thought that he was a witness for Mr. Moody and thereby
10 his client. If he's representing somebody else, under
11 the rules of practice, he needs to state who that is and
12 give us an address. And I'm unclear at this point if
13 Mr. Moody has retained -- if he's a witness for Mr.
14 Moody and his group, or what the status is.

15 ADMINISTRATIVE LAW JUDGE: Dr. Jekanowski, who
16 is your client?

17 DR. JEKANOWSKI: My client is actually Baker
18 Botts law firm, who has coordinated us with the growers
19 who are in opposition to this and then ultimately
20 coordinated with Jim Moody.

21 ADMINISTRATIVE LAW JUDGE: All right. And
22 would you spell the name of the law firm, please?

23 DR. JEKANOWSKI: Yes. It's B-a-k-e-r. Next
24 word is B-o-t-t-s.

25 ADMINISTRATIVE LAW JUDGE: And do you know

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1 their street address as you sit there?

2 DR. JEKANOWSKI: I don't.

3 ADMINISTRATIVE LAW JUDGE: All right, give as
4 much as you can.

5 DR. JEKANOWSKI: It is Washington, D.C., 13th
6 Street.

7 MR. CARSWELL: Your Honor?

8 ADMINISTRATIVE LAW JUDGE: Mr. Carswell?

9 MR. CARSWELL: I happened to -- used to work
10 in that same building. It's 1299 Pennsylvania Avenue,
11 Northwest, Washington, D.C., 20004. And I just wanted
12 clarify, so that no one would think that we're trying to
13 be evasive, one of the growers is funding this work that
14 was done by Mr. Jekanowski is Anheuser-Busch.

15 ADMINISTRATIVE LAW JUDGE: Thank you, Mr.
16 Carswell. All right, Dr. Folwell, would you come to a
17 microphone so that I can ask you if you want to cross-
18 examine tonight and if you don't want to do it tonight,
19 if there's any other time this week when we'll know that
20 Dr. Jekanowski is here that might work better for you
21 and the like? If you'd again state your name for the
22 record.

23 DR. FOLWELL: Raymond Folwell, Washington
24 State University. Actually, I can be here in the
25 morning until 9:30, so if you don't go into a late, late

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1 night session here, I can come back at 8:30 in the
2 morning, but I do have to leave then for Walla Walla.

3 ADMINISTRATIVE LAW JUDGE: Do you believe an
4 hour would be adequate for you to complete the cross-
5 examination you have in mind?

6 DR. FOLWELL: Yes, I do.

7 ADMINISTRATIVE LAW JUDGE: All right. That's
8 what I would prefer to do unless anyone here strongly
9 objects. Mr. Carswell?

10 MR. CARSWELL: I don't strongly object, but I
11 do want to point out as a reminder that Dr. Tweeten is
12 also planning to testify and I don't know if that'll
13 give Dr. Folwell sufficient time to cross-examine him,
14 as well.

15 ADMINISTRATIVE LAW JUDGE: Okay. If he has to
16 leave by 9:30, I just don't think he's going to have a
17 chance to cross-examine Dr. Tweeten, but maybe I
18 shouldn't speak for you, Dr. Folwell. Would you prefer
19 to go forward with your cross-examination of Dr.
20 Jekanowski tonight so that you might have some chance if
21 Dr. Tweeten finishes within the first hour tomorrow to
22 cross-examine him?

23 DR. FOLWELL: My cross-examination's going to
24 be more of a practical nature, not dealing with the
25 hypothetical in relation to this issue, so my cross-

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1 examination on that will be fairly short. I don't know
2 what the other members of the committee who I've had
3 conversations -- what their plans are.

4 ADMINISTRATIVE LAW JUDGE: All right, Mr...

5 DR. FOLWELL: We just discussing -- as a
6 matter of fact, I am not here as a member of their
7 committee. I'm here as a service to the industry.

8 ADMINISTRATIVE LAW JUDGE: Thank you. Mr.
9 Carswell?

10 MR. CARSWELL: Yes. I just believe that
11 having read it, I think Dr. Tweeten's statement will be
12 very short tomorrow, so perhaps if Dr. Folwell could
13 cross-examine Mark tonight, and then Dr. Tweeten spoke
14 first thing in the morning, he could cross-examine Dr.
15 Tweeten first thing in the morning and that would give
16 him a chance to cross-examine both and then maybe we
17 could go back to Mark's cross-examination after that.

18 ADMINISTRATIVE LAW JUDGE: I agree with going
19 back to Dr. Jekanowski's cross-examination, fitting Dr.
20 Tweeten in, but Dr. Folwell, I'll still be guided by
21 whether you would like to do your cross-examination now
22 of Dr. Jekanowski, or hold that until 8:30 in the
23 morning.

24 DR. FOLWELL: Preferring not -- realizing how
25 long I sat in that chair, I'd prefer doing it in the

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1 morning.

2 ADMINISTRATIVE LAW JUDGE: All right, I -- Ms.
3 Deskins?

4 MS. DESKINS: Judge Clifton, if Dr. Tweeten
5 has a statement, could he give it to Dr. Folwell now so
6 he can read it and in the morning perhaps things would
7 proceed quicker?

8 ADMINISTRATIVE LAW JUDGE: Dr. Tweeten, do you
9 have a prepared statement all ready?

10 DR. TWEETEN: Yes, I do.

11 ADMINISTRATIVE LAW JUDGE: How many copies of
12 it do you have right now?

13 DR. TWEETEN: Approximately 15.

14 ADMINISTRATIVE LAW JUDGE: Wonderful. Could
15 you distribute those before we disband for the night?

16 DR. TWEETEN: Yes.

17 ADMINISTRATIVE LAW JUDGE: All right. Very
18 good. Thank you. Excellent suggestion. All right, is
19 there anything further -- now stay in your places if you
20 want to receive one of these copies to be distributed
21 and please raise your hands so Dr. Tweeten will know you
22 want one. Is there anything further, then, while we're
23 still on record?

24 MS. DESKINS: Judge Clifton, I did have one
25 thing. If Dr. Jekanowski has any other exhibits or

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1 documents that he wants to be made put into the record,
2 tonight would be a good time to copy them so in the
3 morning we don't have to worry about getting copies.
4 They'll be ready and we can proceed.

5 ADMINISTRATIVE LAW JUDGE: All right. Thank
6 you. Dr. Jekanowski, are you going to have any
7 additional copies of your report?

8 DR. JEKANOWSKI: Possibly.

9 ADMINISTRATIVE LAW JUDGE: One additional and
10 one for the court reporter for the typist, for sure.

11 MS. DESKINS: Judge Clifton, the reason I
12 asked is I believe when Dr. Folwell testified, he
13 referred to a report from Sparks, and I don't if they
14 plan to introduce it or not, but if they do, having
15 sufficient copies tomorrow would be a great benefit to
16 the hearing moving forward.

17 DR. JEKANOWSKI: Sure. That report was
18 actually a private correspondence with USDA. I think I
19 have copies of it. If I do, I'll be happy to submit it.

20 MS. DESKINS: It's up to them, Your Honor, but
21 I just -- just so that they know if they do want to use
22 it, they need sufficient copies.

23 DR. JEKANOWSKI: Sure. I understand that.

24 ADMINISTRATIVE LAW JUDGE: All right, good.
25 Have the copies of Dr. Tweeten's report been

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1 distributed? Raise your hand if you still need one.
2 All right, I thank you all. I'll see you at 8:30 in the
3 morning. We now go off record at 5:43.

4 ***

5 [End of Proceedings]

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78 HELD AT: Yakima, Washington
910 DATE: October 20, 2003
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